

FIRST BANCORP /PR/
Form 10-Q
May 16, 2011

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2011

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 001-14793

FIRST BANCORP.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

Puerto Rico
(State or other jurisdiction of
incorporation or organization)

66-0561882
(I.R.S. employer
identification number)

1519 Ponce de León Avenue, Stop 23
Santurce, Puerto Rico
(Address of principal executive offices)

00908
(Zip Code)

(787) 729-8200

(Registrant's telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large accelerated
filer

Accelerated filer

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

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common stock: 21,303,669 outstanding as of April 30, 2011.

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Forward Looking Statements

This Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in this Form 10-Q or future filings by First BanCorp (the Corporation) with the Securities and Exchange Commission (SEC), in the Corporation's press releases or in other public or stockholder communications, or in oral statements made with the approval of an authorized executive officer, the word or phrases would be, will allow, intends to, will likely result, are expected to, should, anticipate and similar expressions meant to identify forward-looking statements.

First BanCorp wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made, and represent First BanCorp's expectations of future conditions or results and are not guarantees of future performance. First BanCorp advises readers that various factors could cause actual results to differ materially from those contained in any forward-looking statement. Such factors include, but are not limited to, the following:

uncertainty about whether the Corporation will be able to fully comply with the written agreement dated June 3, 2010 (the Written Agreement) that the Corporation entered into with the Federal Reserve Bank of New York (the FED or Federal Reserve) and the order dated June 2, 2010 (the FDIC Order) and collectively with the Written Agreement, (the Agreements) that the Corporation's banking subsidiary, FirstBank Puerto Rico (FirstBank or the Bank) entered into with the Federal Deposit Insurance Corporation (FDIC) and the Office of the Commissioner of Financial Institutions of the Commonwealth of Puerto Rico (OCIF) that, among other things, require the Bank to attain certain capital levels and reduce its special mention, classified, delinquent and non-accrual assets;

uncertainty as to whether the Corporation will be able to issue \$350 million of equity so as to meet the remaining substantive condition necessary to compel the United States Department of the Treasury (the U.S. Treasury) to convert into common stock the shares of the Corporation's Fixed Rate Cumulative Mandatorily Convertible Preferred Stock, Series G (the Series G Preferred Stock), that the Corporation issued to the U.S. Treasury;

uncertainty as to whether the Corporation will be able to complete any other future capital-raising efforts;

uncertainty as to the availability of certain funding sources, such as retail brokered certificates of deposit (CDs);

the Corporation's reliance on brokered CDs and its ability to obtain, on a periodic basis, approval from the FDIC to issue brokered CDs to fund operations and provide liquidity in accordance with the terms of the Order;

the risk of not being able to fulfill the Corporation's cash obligations or resume paying dividends to the Corporation's stockholders due to the Corporation's inability to receive approval from the FED to receive dividends from the Corporation's banking subsidiary, FirstBank;

the risk of being subject to possible additional regulatory actions;

the strength or weakness of the real estate market and of the consumer and commercial credit sectors and their impact on the credit quality of the Corporation's loans and other assets, including the construction and commercial real estate loan portfolios, which have contributed and may continue to contribute to, among other things, the high levels of non-performing assets, charge-offs and the provision expense and may subject the Corporation to further risk from loan defaults and foreclosures;

adverse changes in general economic conditions in the United States and in Puerto Rico, including the interest rate scenario, market liquidity, housing absorption rates, real estate prices and disruptions in the U.S. capital markets, which may reduce interest margins, impact funding sources and affect demand for all of the Corporation's products and services and the value of the Corporation's assets;

an adverse change in the Corporation's ability to attract new clients and retain existing ones;

a decrease in demand for the Corporation's products and services and lower revenues and earnings because of the continued recession in Puerto Rico and the current fiscal problems and budget deficit of the Puerto Rico government;

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uncertainty about regulatory and legislative changes for financial services companies in Puerto Rico, the United States and the U.S. and British Virgin Islands, which could affect the Corporation's financial performance and could cause the Corporation's actual results for future periods to differ materially from prior results and anticipated or projected results;

uncertainty about the effectiveness of the various actions undertaken to stimulate the U.S. economy and stabilize the U.S. financial markets, and the impact such actions may have on the Corporation's business, financial condition and results of operations;

changes in the fiscal and monetary policies and regulations of the federal government, including those determined by the Federal Reserve, the FDIC, government-sponsored housing agencies and local regulators in Puerto Rico and the U.S. and British Virgin Islands;

the risk of possible failure or circumvention of controls and procedures and the risk that the Corporation's risk management policies may not be adequate;

the risk that the FDIC may further increase the deposit insurance premium and/or require special assessments to replenish its insurance fund, causing an additional increase in our non-interest expense;

the risk of not being able to recover the assets pledged to Lehman Brothers Special Financing, Inc.;

the impact on the Corporation's results of operations and financial condition associated with acquisitions and dispositions;

a need to recognize additional impairments of financial instruments or goodwill relating to acquisitions;

the adverse effect of litigation;

risks that further downgrades in the credit ratings of the Corporation's long-term senior debt will adversely affect the Corporation's ability to make future borrowings;

the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) on our businesses, business practices and cost of operations;

general competitive factors and industry consolidation; and

the future dilution to holders of the Corporation's common stock resulting from additional issuances of common stock or securities convertible into common stock.

The Corporation does not undertake, and specifically disclaims any obligation, to update any of the forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements except as required by the federal securities laws.

Investors should refer to the Corporation's Annual Report on Form 10-K for the year ended December 31, 2010 for a discussion of such factors and certain risks and uncertainties to which the Corporation is subject.

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FIRST BANCORP
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(Unaudited)

(In thousands, except for share information)	March 31, 2011	December 31, 2010
ASSETS		
Cash and due from banks	\$ 663,581	\$ 254,723
Money market investments:		
Federal funds sold	5,382	6,236
Time deposits with other financial institutions	1,355	1,346
Other short-term investments	202,976	107,978
Total money market investments	209,713	115,560
Investment securities available for sale, at fair value:		
Securities pledged that can be repledged	1,667,261	1,344,873
Other investment securities	1,056,906	1,399,580
Total investment securities available for sale	2,724,167	2,744,453
Investment securities held to maturity, at amortized cost:		
Securities pledged that can be repledged		239,553
Other investment securities		213,834
Total investment securities held to maturity (2010-fair value of \$476,516)		453,387
Other equity securities	99,060	55,932
Loans, net of allowance for loan and lease losses of \$561,695 (2010 - \$553,025)	10,528,080	11,102,411
Loans held for sale, at lower of cost or market	305,494	300,766
Total loans, net	10,833,574	11,403,177
Premises and equipment, net	206,863	209,014
Other real estate owned	91,948	84,897
Accrued interest receivable on loans and investments	55,580	59,061
Due from customers on acceptances	598	1,439
Other assets	219,006	211,434

Total assets	\$	15,104,090	\$	15,593,077
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LIABILITIES

Deposits:

Non-interest-bearing deposits	\$	707,938	\$	668,052
Interest-bearing deposits		11,008,498		11,391,058

Total deposits		11,716,436		12,059,110
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Securities sold under agreements to repurchase		1,400,000		1,400,000
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Advances from the Federal Home Loan Bank (FHLB)		540,440		653,440
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Notes payable (including \$12,437 and \$11,842 measured at fair value as of March 31, 2011 and December 31, 2010, respectively)		27,837		26,449
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Other borrowings		231,959		231,959
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Bank acceptances outstanding		598		1,439
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Accounts payable and other liabilities		159,551		162,721
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Total liabilities		14,076,821		14,535,118
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Commitments and Contingencies (Note 22)

STOCKHOLDERS EQUITY

Preferred stock, authorized 50,000,000 shares: issued 22,828,174; outstanding 2,946,046; aggregate liquidation value of \$487,221:

Fixed Rate Cumulative Mandatorily Convertible Preferred Stock: issued and outstanding 424,174 shares		363,677		361,962
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Non-cumulative Perpetual Monthly Income Preferred Stock: issued 22,004,000 shares and outstanding 2,521,872 shares		63,047		63,047
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Common stock, \$0.10 par value, authorized 2,000,000,000 shares; issued 21,963,522 shares		2,196		2,196
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Less: Treasury stock (at par value)		(66)		(66)
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Common stock outstanding, 21,303,669 shares outstanding		2,130		2,130
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Additional paid-in capital		319,483		319,459
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Legal surplus		299,006		299,006
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Accumulated deficit		(35,498)		(5,363)
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Accumulated other comprehensive income, net of tax expense of \$5,205 (December 31, 2010 - \$5,351)		15,424		17,718
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Total stockholders equity		1,027,269		1,057,959
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Total liabilities and stockholders equity	\$	15,104,090	\$	15,593,077
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The accompanying notes are an integral part of these statements.

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FIRST BANCORP
CONSOLIDATED STATEMENTS OF LOSS
(Unaudited)

	Quarter Ended	
	March 31, 2011	March 31, 2010
(In thousands, except per share data)		
Interest income:		
Loans	\$ 157,971	\$ 177,433
Investment securities	22,623	43,119
Money market investments	309	436
Total interest income	180,903	220,988
Interest expense:		
Deposits	54,059	65,966
Loans payable		2,177
Federal funds purchased and securities sold under agreements to repurchase	13,136	25,282
Advances from FHLB	4,745	7,694
Notes payable and other borrowings	2,684	3,006
Total interest expense	74,624	104,125
Net interest income	106,279	116,863
Provision for loan and lease losses	88,732	170,965
Net interest income (loss) after provision for loan and lease losses	17,547	(54,102)
Non-interest income:		
Other service charges on loans	1,718	1,756
Service charges on deposit accounts	3,332	3,468
Mortgage banking activities	6,591	2,500
Net gain on sale of investments, net of impairments on equity securities	19,341	30,764
Other non-interest income	9,503	6,838
Total non-interest income	40,485	45,326
Non-interest expenses:		
Employees compensation and benefits	30,439	31,728
Occupancy and equipment	15,250	14,851
Business promotion	2,664	2,205
Professional fees	5,137	5,287
Taxes, other than income taxes	3,255	3,821

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Insurance and supervisory fees	15,177	18,518
Net loss on real estate owned (REO) operations	5,500	3,693
Other non-interest expenses	5,444	11,259
Total non-interest expenses	82,866	91,362
Loss before income taxes	(24,834)	(100,138)
Income tax expense	(3,586)	(6,861)
Net loss	\$ (28,420)	\$ (106,999)
Net loss attributable to common stockholders	\$ (35,437)	\$ (113,151)
Net loss per common share:		
Basic	\$ (1.66)	\$ (18.34)
Diluted	\$ (1.66)	\$ (18.34)
Dividends declared per common share	\$	\$

The accompanying notes are an integral part of these statements.

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FIRST BANCORP
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Quarter Ended	
	March	March 31,
	31,	2010
(In thousands)	2011	2010
Cash flows from operating activities:		
Net Loss	\$ (28,420)	\$ (106,999)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation	5,810	5,171
Amortization and impairment of core deposit intangible	589	666
Provision for loan and lease losses	88,732	170,965
Deferred income tax expense	1,746	4,076
Stock-based compensation recognized	24	24
Gain on sale of investments, net	(18,710)	(31,364)
Other-than-temporary impairments on investment securities		600
Derivatives instruments and hedging activities loss	518	1,733
Gain on sale of assets FB Insurance VI	(2,845)	
Net gain on sale of loans and impairments	(5,505)	(220)
Net amortization of premiums and discounts on deferred loan fees and costs	395	246
Net increase in mortgage loans held for sale	(1,382)	(4,385)
Amortization of broker placement fees	5,359	5,465
Net amortization of premium and discounts on investment securities	1,736	968
Increase in accrued income tax payable	1,642	2,384
Decrease in accrued interest receivable	3,481	8,517
Decrease in accrued interest payable	(22)	(417)
(Increase) decrease in other assets	(2,355)	13,208
(Decrease) increase in other liabilities	(7,145)	12,659
Total adjustments	72,068	190,296
Net cash provided by operating activities	43,648	83,297
Cash flows from investing activities:		
Principal collected on loans	569,498	1,050,262
Loans originated	(503,164)	(565,515)
Purchases of loans	(32,728)	(41,893)
Proceeds from sale of loans	330,978	19,064
Proceeds from sale of repossessed assets	21,920	19,575
Proceeds from sale of available-for-sale securities	41,422	393,433
Proceeds from sale of held-to-maturity securities	348,798	
Purchases of securities available for sale		(99,867)
Proceeds from principal repayments and maturities of securities held to maturity	33,726	35,998

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Proceeds from principal repayments and maturities of securities available for sale	106,117	423,747
Additions to premises and equipment	(3,810)	(6,278)
Proceeds from sale of other investment securities		5,602
Proceeds from sale of assets FB Insurance VI	2,940	
Proceeds from securities litigations settlement	631	
Decrease in other equity securities	4,500	
Net cash provided by investing activities	920,828	1,234,128
Cash flows from financing activities:		
Net (decrease) increase in deposits	(348,465)	203,321
Net decrease in loans payable		(300,000)
Net decrease in securities sold under agreements to repurchase		(576,631)
Net FHLB advances paid	(113,000)	(18,000)
Net cash used in financing activities	(461,465)	(691,310)
Net increase in cash and cash equivalents	503,011	626,115
Cash and cash equivalents at beginning of period	370,283	704,084
Cash and cash equivalents at end of period	\$ 873,294	\$ 1,330,199
Cash and cash equivalents include:		
Cash and due from banks	\$ 663,581	\$ 675,551
Money market instruments	209,713	654,648
	\$ 873,294	\$ 1,330,199

The accompanying notes are an integral part of these statements.

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FIRST BANCORP
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY
(Unaudited)

(In thousands)	Quarter Ended	
	March 31, 2011	March 31, 2010
Preferred Stock:		
Balance at beginning of period	\$ 425,009	\$ 928,508
Accretion of preferred stock discount	1,715	1,152
Balance at end of period	426,724	929,660
Common Stock outstanding	2,130	6,169
Additional Paid-In-Capital:		
Balance at beginning of period	319,459	220,596
Stock-based compensation recognized	24	24
Balance at end of period	319,483	220,620
Legal Surplus	299,006	299,006
(Accumulated deficit) Retained Earnings :		
Balance at beginning of period	(5,363)	118,291
Net loss	(28,420)	(106,999)
Cash dividends declared on common stock		
Cash dividends declared on preferred stock		
Accretion of preferred stock discount	(1,715)	(1,152)
Balance at end of period	(35,498)	10,140
Accumulated Other Comprehensive Income (Loss), net of tax:		
Balance at beginning of period	17,718	26,493
Other comprehensive loss, net of tax	(2,294)	(3,545)
Balance at end of period	15,424	22,948
Total stockholders equity	\$ 1,027,269	\$ 1,488,543

The accompanying notes are an integral part of these statements.

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FIRST BANCORP
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Unaudited)

	Quarter Ended	
	March 31, 2011	March 31, 2010
Net loss	\$ (28,420)	\$ (106,999)
Other comprehensive loss:		
Unrealized gains and losses on available-for-sale securities:		
Unrealized holding (losses) gains arising during the period	(5,181)	17,529
Reclassification adjustments for net gain included in net income	(48)	(20,696)
Reclassification adjustments for other-than-temporary impairment on equity securities		350
Net unrealized gains on securities reclassified from held to maturity to available for sale	2,789	
Income tax benefit (expense) related to items of other comprehensive income	146	(728)
Other comprehensive loss for the period, net of tax	(2,294)	(3,545)
Total comprehensive loss	\$ (30,714)	\$ (110,544)

The accompanying notes are an integral part of these statements.

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FIRST BANCORP
PART I NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1 BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

The Consolidated Financial Statements (unaudited) have been prepared in conformity with the accounting policies stated in the Corporation's Audited Consolidated Financial Statements included in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2010. Certain information and note disclosures normally included in the financial statements prepared in accordance with generally accepted accounting principles in the United States of America (GAAP) have been condensed or omitted from these statements pursuant to the rules and regulations of the SEC and, accordingly, these financial statements should be read in conjunction with the Audited Consolidated Financial Statements of the Corporation for the year ended December 31, 2010, included in the Corporation's 2010 Annual Report on Form 10-K. All adjustments (consisting only of normal recurring adjustments) that are, in the opinion of management, necessary for a fair presentation of the statement of financial position, results of operations and cash flows for the interim periods have been reflected. All significant intercompany accounts and transactions have been eliminated in consolidation.

The results of operations for the quarter ended March 31, 2011 are not necessarily indicative of the results to be expected for the entire year.

All share and per share amounts of common shares included in the consolidated financial statements have been adjusted to retroactively reflect the 1-for-15 reverse stock split effected January 7, 2011.

Capital and Liquidity

The consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the discharge of liabilities in the normal course of business for the foreseeable future. Sustained weak economic conditions that have severely affected Puerto Rico and the United States over the last several years have adversely impacted First BanCorp's and FirstBank's results of operations and capital levels. The significant loss in 2010, primarily related to credit losses (including losses associated with adversely classified loans and non-performing loans transferred to held for sale), the increase in the deposit insurance premium expense and increases to the deferred tax asset valuation allowance reduced the Corporation's and the Bank's capital levels during 2010. The net loss for the first quarter of 2011 was primarily related to credit losses. As of March 31, 2011, the Corporation's Total Capital, Tier 1 Capital and Leverage ratios were 11.97%, 10.65% and 7.78%, respectively, compared to 12.02%, 10.73% and 7.57%, respectively, as of December 31, 2010. Meanwhile, FirstBank's Total Capital, Tier 1 Capital and Leverage ratios as of March 31, 2011 were 11.71%, 10.40% and 7.60%, respectively, up from 11.57%, 10.28% and 7.25%, respectively, as of December 31, 2010. The improvement in the capital ratios for FirstBank was primarily related to a \$22 million capital contribution from the holding company.

As described in Note 17, Regulatory Matters, FirstBank is currently operating under a Consent Order (the FDIC Order) with the FDIC and the OCIF and First BanCorp has entered into a Written Agreement (the Written Agreement and collectively with the Order the Agreements) with the Federal Reserve. The minimum capital ratios established by the FDIC Order are 8% for Leverage (Tier 1 Capital to Average Total Assets), 10% for Tier 1 Capital to Risk-Weighted Assets and 12% for Total Capital to Risk-Weighted Assets. The FDIC Order does not contain a specific date for achieving the minimum capital ratios.

The Corporation is working to complete a capital raise to ensure that the projected level of regulatory capital can support its balance sheet over the long-term. As part of the Corporation's capital raising efforts, the Corporation has been engaged in conversations with a number of entities, including private equity firms. The issuance of additional equity securities and other capital management or business strategies could depress the market price of our common stock and result in the dilution of our common stockholders.

In March 2011, the Corporation submitted an updated Capital Plan (the Capital Plan) to the regulators. The Capital Plan contemplates a \$350 million capital raise through the issuance of new common shares for cash, and other actions to further reduce the Corporation's and the Bank's risk-weighted assets, strengthen their capital positions and meet the minimum capital ratios required under the FDIC Order. Among the strategies contemplated in the Capital Plan are further reduction of the Corporation's loan portfolio and investment portfolio. The Capital Plan identified specific

targeted Leverage, Tier 1 Capital to Risk-Weighted Assets and Total Capital to Risk-Weighted Assets ratios to be achieved by the Bank each calendar quarter until the capital levels required under the FDIC Order are achieved. As of March 31, 2011, all capital ratios for FirstBank are above the targeted capital levels and the Corporation expects to be in compliance with the minimum capital ratios under the FDIC Order by June 30, 2011.

If the Bank fails to achieve the capital ratios as provided in the FDIC Order, within 45 days of being out of compliance, the Bank would be required to increase capital in an amount sufficient to comply with the capital ratios set forth in the Capital Plan, or submit to

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the regulators a contingency plan for the sale, merger, or liquidation of the institution in the event the primary sources of capital are not available. Thereafter the FDIC would determine whether and when to initiate an acceptable contingency plan.

Should the Corporation's efforts to raise capital not be completed, the Corporation's Capital Plan includes other actions which could allow the Bank to attain the minimum capital ratios under the FDIC Order. The strategies incorporated into the Capital Plan to meet the minimum capital ratios include the following:

Strategies completed during the first quarter of 2011:

Sale of performing first lien residential mortgage loans The Bank sold approximately \$236 million in mortgage loans to another financial institution during February 2011. Proceeds were used, in part, to reduce funding sources and to support liquidity reserves.

Sale of Investment securities The Bank sold approximately \$330 million in investment securities during March 2011. Proceeds were used, in part, to reduce funding sources and to support liquidity reserves.

The Corporation contributed \$22 million of capital to the Bank during March 2011.

Strategies completed or expected to be completed by June 30, 2011:

Sale of performing first lien residential mortgage loans- The Bank entered into a letter of intent to sell mortgage loans before June 30, 2011. During the first quarter of 2011, the Corporation reclassified from held for investment to held for sale approximately \$282 million related to this transaction. The loans were sold in April 2011.

Sale of investment securities The Bank sold approximately \$268 million in investment securities on April 6, 2011.

Sale of commercial loan participations The Bank has commenced negotiations to sell approximately \$150 million in loan participations to other financial institutions by June 30, 2011.

The proceeds received from the above three transactions will be used to reduce funding sources.

Upon the successful completion of these actions, when combined with the achievement of operating results in line with management's current expectations, management expects that the Corporation and the Bank will attain the minimum capital ratios set forth in the Capital Plan. However, no assurance can be given that the Corporation and the Bank will be able to achieve such ratios.

In the event the Corporation is unable to complete its capital raising efforts during 2011 and actual credit losses exceed amounts projected, the Capital Plan includes additional actions designed to allow the Bank to maintain the minimum capital ratios for the foreseeable future, including the sale of additional assets.

Both the Corporation and the Bank actively manage liquidity and cash flow needs. The Corporation suspended common and preferred dividends to stockholders since August 2009. As of March 31, 2011, the holding company had \$19.8 million of cash and cash equivalents. Cash and cash equivalents at the Bank as of March 31, 2011 were approximately \$873.3 million. The Bank has \$100 million, \$187 million and \$15.4 million, in repurchase agreements, FHLB advances and notes payable, respectively, maturing over the next twelve months. In addition, it had \$5.7 billion in brokered CDs as of March 31, 2011, of which \$3.0 billion mature over the next twelve months. Liquidity at the Bank level is highly dependent on bank deposits, which fund 77.82% of the Bank's assets (or 39.91% excluding brokered CDs). The Corporation has continued to issue brokered CDs pursuant to approvals received from the FDIC to renew or roll over certain amounts of brokered CDs through June 30, 2011. Management cannot be certain it will continue to obtain waivers from the restrictions to issue brokered CDs under the FDIC Order to meet its obligations and execute its business plans. As of March 31, 2011, the Bank held approximately \$332 million of readily pledgeable or sellable investment securities. As previously noted above, the Corporation plans to sell certain loans and investments in 2011 to that would allow it to meet and maintain minimum capital ratios required by the FDIC Order. Based on current and expected liquidity needs and sources, management expects First BanCorp to be able to meet its

obligations for a reasonable period of time. During 2010, the Corporation and the Bank suffered credit downgrades. The Bank suffered a further downgrade in April 2011. The Corporation does not have any outstanding debt or derivative agreements that would be affected by the credit downgrades. Furthermore, given our non-reliance on corporate debt or other instruments directly linked in terms of pricing or volume to credit ratings, the liquidity of the Corporation so far has not been affected in any material way by the downgrades. The Corporation's ability to access new non-deposit funding, however, could be adversely affected by these downgrades and any additional downgrades.

If unanticipated market factors emerge, such as a significant increase in the provision for loan and lease losses, or if the Corporation is unable to raise additional capital or complete identified capital preservation initiatives, successfully execute its strategic operating plans, issue a sufficient amount of brokered CDs or comply with the FDIC Order, its banking regulators could take further action, which could include actions that may have a material adverse effect on the Bank's business, results of operations and financial position, including the appointment of a conservator or receiver.

Table of Contents**Adoption of new accounting requirements and recently issued but not yet effective accounting requirements**

The Financial Accounting Standards Board (FASB) has issued the following accounting pronouncements and guidance relevant to the Corporation's operations:

In December 2010, the FASB updated the Accounting Standards Codification (Codification) to modify Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. As a result, current GAAP will be improved by eliminating an entity's ability to assert that a reporting unit is not required to perform Step 2 because the carrying amount of the reporting unit is zero or negative despite the existence of qualitative factors that indicate the goodwill is more likely than not impaired. As a result, goodwill impairments may be reported sooner than under current practice. The objective of this Update is to address questions about entities with reporting units with zero or negative carrying amounts because some entities concluded that Step 1 of the test is passed in those circumstances because the fair value of their reporting unit will generally be greater than zero. As a result of that conclusion, some constituents raised concerns that Step 2 of the test is not performed despite factors indicating that goodwill may be impaired. The amendments in this Update do not provide guidance on how to determine the carrying amount or measure the fair value of the reporting unit. For public entities, the amendments in this Update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. Early adoption is not permitted. The adoption of this guidance did not have an impact on the Corporation's financial statements.

In December 2010, the FASB updated the Codification to clarify required disclosures of supplementary pro forma information for business combinations. The amendments specify that, if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the year had occurred as of the beginning of the comparable prior annual period only. Additionally, the Update expands disclosures to include a description of the nature and amount of material nonrecurring pro forma adjustments directly attributable to the business combination included in the pro forma revenue and earnings. This guidance is effective for reporting periods beginning after December 15, 2010; early adoption is permitted. The Corporation adopted this guidance with no impact on the financial statements.

In April 2011, the FASB updated the Codification to clarify the guidance on a creditor's evaluation of whether a restructuring constitutes a troubled debt restructuring (TDR). Under the amendments, a creditor must separately conclude that a loan modification constitutes a concession and that the debtor is experiencing financial difficulties when evaluating whether a loan modification constitutes a TDR. If a creditor determines that it has granted a concession to a debtor, the creditor must make a separate assessment about whether the debtor is experiencing financial difficulties to determine whether the restructuring constitutes a TDR. The amendments clarify the guidance on a creditor's evaluation of whether it has granted a concession and what constitutes financial difficulty. In addition, the amendments clarify that a creditor is precluded from using the effective interest rate test in the debtor's guidance on restructuring of payables when evaluating whether a restructuring constitutes a TDR. The amendments in this Update are effective for the first interim or annual period beginning on or after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. The Corporation is currently evaluating the impact of the adoption of this guidance on the financial statements.

In April 2011, the FASB updated the Codification to improve the accounting for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The amendments in this Update remove from the assessment of effective control the criterion relating to the transferor's ability to repurchase or redeem financial assets on substantially the agreed terms, even in the event of default by the transferee. The Board concluded that this criterion is not a determining factor of effective control. Consequently, the amendments in this Update also eliminate the requirement to demonstrate that the transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets. Eliminating the transferor's ability criterion and related implementation guidance from an entity's assessment of effective control should improve the accounting for repurchase agreements and other similar transactions. The amendments in this Update are effective for the first interim or annual period beginning on or after December 15, 2011, and should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted. The Corporation is currently evaluating the impact of the adoption of this guidance on the financial statements.

Table of Contents**2 EARNINGS PER COMMON SHARE**

The calculations of earnings per common share for the quarters ended on March 31, 2011 and 2010 are as follows:

	Quarter Ended	
	March 31, 2011	March 31, 2010
	(In thousands, except per share data)	
Net loss:		
Net loss	\$ (28,420)	\$ (106,999)
Cumulative non-convertible preferred stock dividends (Series F)		(5,000)
Cumulative convertible preferred stock dividend (Series G)	(5,302)	
Preferred stock discount accretion (Series G and F)	(1,715)	(1,152)
Net loss attributable to common stockholders	\$ (35,437)	\$ (113,151)
Average common shares outstanding ⁽¹⁾	21,303	6,168
Average potential common shares ⁽¹⁾		
Average common shares outstanding- assuming dilution ⁽¹⁾	21,303	6,168
Basic loss per common share ⁽¹⁾	\$ (1.66)	\$ (18.34)
Diluted loss per common share ⁽¹⁾	\$ (1.66)	\$ (18.34)

(1) All share and per share data has been adjusted to retroactively reflect the 1-for-15 reverse stock split effected January 7, 2011.

Loss per common share is computed by dividing net loss attributable to common stockholders by the weighted average common shares issued and outstanding. Net loss attributable to common stockholders represents net loss adjusted for preferred stock dividends including dividends declared, and cumulative dividends related to the current dividend period that have not been declared as of the end of the period, and the accretion of discount on preferred stock issuances. Basic weighted average common shares outstanding exclude unvested shares of restricted stock.

Potential common shares consist of common stock issuable under the assumed exercise of stock options, unvested shares of restricted stock, and outstanding warrants using the treasury stock method. This method assumes that the potential common shares are issued and the proceeds from the exercise, in addition to the amount of compensation cost attributable to future services, are used to purchase common stock at the exercise date. The difference between the number of potential shares issued and the shares purchased is added as incremental shares to the actual number of shares outstanding to compute diluted earnings per share. Stock options, unvested shares of restricted stock, and outstanding warrants that result in lower potential shares issued than shares purchased under the treasury stock method are not included in the computation of dilutive earnings per share since their inclusion would have an antidilutive effect on earnings per share. For the quarters ended March 31, 2011 and 2010, there were 131,532 and 163,687 outstanding stock options, respectively; warrants outstanding to purchase 389,483 shares of common stock and 716 and 1,432 unvested shares of restricted stock, respectively, that were excluded from the computation of diluted earnings per common share because their inclusion would have an antidilutive effect.

3 STOCK OPTION PLAN

Between 1997 and January 2007, the Corporation had a stock option plan (the 1997 stock option plan) that authorized the granting of up to 579,740 options on shares of the Corporation's common stock to eligible employees.

The options granted under the plan could not exceed 20% of the number of common shares outstanding. Each option provides for the purchase of one share of common stock at a price not less than the fair market value of the stock on the date the option was granted. Stock options were fully vested upon grant. The maximum term to exercise the options is ten years. The stock option plan provides for a proportionate adjustment in the exercise price and the number of shares that can be purchased in the event of a stock dividend, stock split, reclassification of stock, merger or reorganization and certain other issuances and distributions such as stock appreciation rights.

Under the 1997 stock option plan, the Compensation and Benefits Committee (the Compensation Committee) had the authority to grant stock appreciation rights at any time subsequent to the grant of an option. Pursuant to stock appreciation rights, the optionee surrenders the right to exercise an option granted under the plan in consideration for payment by the Corporation of an amount equal to the excess of the fair market value of the shares of common stock subject to such option surrendered over the total option price of such shares. Any option surrendered is cancelled by the Corporation and the shares subject to the option are not eligible for further

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grants under the option plan. On January 21, 2007, the 1997 stock option plan expired; all outstanding awards granted under this plan continue in full force and effect, subject to their original terms. No awards for shares could be granted under the 1997 stock option plan as of its expiration.

On April 29, 2008, the Corporation's stockholders approved the First BanCorp 2008 Omnibus Incentive Plan (the Omnibus Plan). The Omnibus Plan provides for equity-based compensation incentives (the awards) through the grant of stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, and other stock-based awards. This plan allows the issuance of up to 253,333 shares of common stock, subject to adjustments for stock splits, reorganizations and other similar events. The Corporation's Board of Directors, upon receiving the relevant recommendation of the Compensation Committee, has the power and authority to determine those eligible to receive awards and to establish the terms and conditions of any awards subject to various limits and vesting restrictions that apply to individual and aggregate awards. During the fourth quarter of 2008, the Corporation granted 2,412 shares of restricted stock with a fair value of \$130.35 under the Omnibus Plan to the Corporation's independent directors. Of the original 2,412 shares of restricted stock, 268 were forfeited in the second half of 2009, 1,424 vested and, as of March 31, 2011, 720 remain restricted.

For the quarters ended March 31, 2011 and 2010, the Corporation recognized \$23,333 of stock-based compensation expense related to the aforementioned restricted stock awards. The total unrecognized compensation cost related to the non-vested restricted shares was \$62,223 as of March 31, 2011 which expected to be recognized over the next eight months.

The Corporation accounts for stock options using the modified prospective method. There were no stock options granted during 2011 and 2010, therefore no compensation associated with stock options was recorded in those years. No stock options were exercised during the first quarter of 2011 or in 2010.

Stock-based compensation accounting guidance requires the Corporation to develop an estimate of the number of share-based awards that will be forfeited due to employee or director turnover. Quarterly changes in the estimated forfeiture rate may have a significant effect on share-based compensation, as the effect of adjusting the rate for all expense amortization is recognized in the period in which the forfeiture estimate is changed. If the actual forfeiture rate is higher than the estimated forfeiture rate, then an adjustment is made to increase the estimated forfeiture rate, which will result in a decrease to the expense recognized in the financial statements. If the actual forfeiture rate is lower than the estimated forfeiture rate, then an adjustment is made to decrease the estimated forfeiture rate, which will result in an increase to the expense recognized in the financial statements. When unvested options or shares of restricted stock are forfeited, any compensation expense previously recognized on the forfeited awards is reversed in the period of the forfeiture.

Stock options outstanding as of March 31, 2011 follows:

	Quarter Ended March 31, 2011			
	Number of Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (In thousands)
End of period outstanding and exercisable	131,532	\$ 202.91	4.28	\$

Table of Contents**4 INVESTMENT SECURITIES****Investment Securities Available for Sale**

The amortized cost, non-credit loss component of other-than-temporary impairment (OTTI) on securities recorded in other comprehensive income (OCI), gross unrealized gains and losses recorded in OCI, approximate fair value, weighted-average yield and contractual maturities of investment securities available for sale as of March 31, 2011 and December 31, 2010 were as follows:

	March 31, 2011					December 31, 2010				
	Amortized cost	Non-Credit Loss Component of OTTI Recorded in OCI	Gross Unrealized gains losses	Fair value	Weighted average yield %	Amortized cost	Non-Credit Loss Component of OTTI Recorded in OCI	Gross Unrealized gains losses	Fair value	Weighted average yield %
Treasury securities: within one year	\$ 58,430	\$	\$ 329	\$	0.91	\$	\$	\$	\$	
1 to 5 years	550,081		6,953	557,034	1.37	599,987		8,727	608,714	
Municipal bonds: within one year										
1 to 5 years	554,322		2,398	551,693	1.09	604,630		2,714	603,353	
Government insured securities: within one year	709		16	725	6.68					
1 to 5 years	38,613		1,350	39,963	5.08	26,768		522	27,290	
5 to 10 years	111,374		276	111,648	5.21	104,352		432	104,784	
10 years	9,458		60	9,518	5.87	4,746		21	4,767	
United States and Puerto Rico Government bonds: within one year										
1 to 5 years	1,322,987		11,382	1,329,340	1.70	1,340,483		12,416	1,348,908	
Mortgage-backed securities: RMBS certificates: within one year										
1 to 5 years	2,043		32	2,075	3.79					
10 years	1,533		101	1,634	5.00	1,716		101	1,817	

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	3,576		133		3,709	4.31	1,716		101		1,817
IA											
ificates:											
within one											
	15				15	6.18	30				30
1 to 5 years	243		11		254	3.90					
5 to											
years	1,015		61		1,076	5.06	1,319		74		1,393
10 years	933,292		29,245	2,545	959,992	4.24	962,246		31,105	3,396	989,955
	934,565		29,317	2,545	961,337	4.24	963,595		31,179	3,396	991,378
IA											
ificates:											
1 to 5 years	2,062		101		2,163	3.86					
5 to											
years	96,630		5,117		101,747	4.36	75,547		3,987		79,534
10 years	139,002		8,682		147,684	5.48	126,847		8,678		135,525
	237,694		13,900		251,594	5.01	202,394		12,665		215,059
ateralized											
gage											
gations											
d or											
anted by											
MC, FNMA											
GNMA:											
10 years	107,222		1,268		108,490	0.99	112,989		1,926		114,915
r mortgage											
through trust											
ificates:											
10 years	95,417	27,063	1		68,355	2.04	100,130	27,814	1		72,317
gage-backed											
ities	1,378,474	27,063	44,619	2,545	1,393,485	3.97	1,380,824	27,814	45,872	3,396	1,395,486
orate bonds:											
10 years	2,000			705	1,295	5.80					
y securities	77			30	47		77		18		59
out											
actual											

ity) (1)

investment												
ities												
able for sale	\$ 2,703,538	\$ 27,063	\$ 56,001	\$ 8,309	\$ 2,724,167	2.86	\$ 2,721,384	\$ 27,814	\$ 58,288	\$ 7,405	\$ 2,744,453	

(1) Represents common shares of other financial institutions in Puerto Rico.

Maturities of mortgage-backed securities are based on contractual terms assuming no prepayments. Expected maturities of investments might differ from contractual maturities because they may be subject to prepayments and/or call options as was the case with \$50 million of U.S. agency debt securities called during 2011. The weighted-average yield on investment securities available for sale is based on amortized cost and, therefore, does not give effect to changes in fair value. The net unrealized gain or loss on securities available for sale and the non-credit loss component of OTTI are presented as part of OCI.

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The following tables show the Corporation's available-for-sale investments' fair value and gross unrealized losses, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of March 31, 2011 and December 31, 2010. It also includes debt securities for which an OTTI was recognized and only the amount related to a credit loss was recognized in earnings:

	Less than 12 months		As of March 31, 2011 12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(In thousands)			
Debt securities:						
U.S. Government agencies obligations	\$ 247,990	\$ 5,027	\$	\$	\$ 247,990	\$ 5,027
Puerto Rico Government obligations	99,998	2			99,998	2
Mortgage-backed securities:						
GNMA	196,374	2,545			196,374	2,545
Other mortgage pass-through trust certificates			68,145	27,063	68,145	27,063
Corporate bonds			1,295	705	1,295	705
Equity securities	47	30			47	30
	\$ 544,409	\$ 7,604	\$ 69,440	\$ 27,768	\$ 613,849	\$ 35,372

	Less than 12 months		As of December 31, 2010 12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(In thousands)			
Debt securities:						
U.S. Government agencies obligations	\$ 249,026	\$ 3,991	\$	\$	\$ 249,026	\$ 3,991
Mortgage-backed securities:						
GNMA	192,799	3,396			192,799	3,396
Other mortgage pass-through trust certificates			72,101	27,814	72,101	27,814
Equity securities	59	18			59	18
	\$ 441,884	\$ 7,405	\$ 72,101	\$ 27,814	\$ 513,985	\$ 35,219

Table of Contents**Investments Held to Maturity**

On March 7, 2011, the Corporation sold \$330 million of mortgage-backed securities that were originally intended to be held to maturity, consistent with deleveraging initiatives included in the Corporation's Capital Plan. The Corporation realized a gain of \$18.7 million associated with this transaction. After the sale, in line with the Corporation's ongoing capital management strategy, the remaining \$89 million of investment securities held in the held-to-maturity portfolio was reclassified to the available-for-sale portfolio.

The amortized cost, gross unrealized gains and losses, approximate fair value, weighted-average yield and contractual maturities of investment securities held to maturity as of December 31, 2010 were as follows:

	Amortized cost	December 31, 2010		Fair value	Weighted average yield%
		Gross Unrealized gains	losses		
(Dollars in thousands)					
U.S. Treasury securities:					
Due within 1 year	\$ 8,487	\$ 5	\$	\$ 8,492	0.30
Puerto Rico Government obligations:					
After 5 to 10 years	19,284	795		20,079	5.87
After 10 years	4,665	49		4,714	5.50
United States and Puerto Rico Government obligations	32,436	849		33,285	4.36
Mortgage-backed securities:					
FHLMC certificates:					
After 1 to 5 years	2,569	42		2,611	3.71
FNMA certificates:					
After 1 to 5 years	2,525	130		2,655	3.86
After 5 to 10 years	391,328	21,946		413,274	4.48
After 10 years	22,529	885		23,414	5.33
Mortgage-backed securities	418,951	23,003		441,954	4.52
Corporate bonds:					
After 10 years	2,000		723	1,277	5.80
Total investment securities held-to-maturity	\$ 453,387	\$ 23,852	\$ 723	\$ 476,516	4.51

Maturities of mortgage-backed securities are based on contractual terms assuming no prepayments. Expected maturities of investments might differ from contractual maturities because they may be subject to prepayments and/or call options.

From time to time the Corporation has securities held to maturity with an original maturity of three months or less that are considered cash and cash equivalents and classified as money market investments in the Consolidated Statement of Financial Condition. As of March 31, 2011, the Corporation had no outstanding securities held to maturity that were classified as cash and cash equivalents.

The following tables show the Corporation's held-to-maturity investments' fair value and gross unrealized losses, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of December 31, 2010:

	As of December 31, 2010					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
Corporate bonds	\$	\$	\$ 1,277	\$ 723	\$ 1,277	\$ 723

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Assessment for OTTI

On a quarterly basis, the Corporation performs an assessment to determine whether there have been any events or economic circumstances indicating that a security with an unrealized loss has suffered OTTI. A debt security is considered impaired if the fair value is less than its amortized cost basis at the reporting date. The accounting literature requires the Corporation to assess whether the unrealized loss is other-than-temporary.

Prior to April 1, 2009, unrealized losses that were determined to be temporary were recorded, net of tax, in other comprehensive income for available-for-sale securities, whereas unrealized losses related to held-to-maturity securities determined to be temporary were not recognized. Regardless of whether the security was classified as available-for-sale or held to maturity, unrealized losses that were determined to be other-than-temporary were recorded through earnings. An unrealized loss was considered other-than-temporary if (i) it was probable that the holder would not collect all amounts due according to the contractual terms of the debt security, or (ii) the fair value was below the amortized cost of the debt security for a prolonged period of time and the Corporation did not have the positive intent and ability to hold the security until recovery or maturity.

OTTI losses for debt securities must be recognized in earnings if an investor has the intent to sell the debt security or it is more likely than not that it will be required to sell the debt security before recovery of its amortized cost basis. However, even if an investor does not expect to sell a debt security, it must evaluate expected cash flows to be received and determine if a credit loss has occurred.

An unrealized loss is generally deemed to be other-than-temporary and a credit loss is deemed to exist if the present value of the expected future cash flows is less than the amortized cost basis of the debt security. The credit loss component of an OTTI, if any, is recorded as a component of Net impairment losses on investment securities in the accompanying consolidated statements of (loss) income, while the remaining portion of the impairment loss is recognized in OCI, provided the Corporation does not intend to sell the underlying debt security and it is more likely than not that the Corporation will not have to sell the debt security prior to recovery.

Debt securities issued by U.S. government agencies, government-sponsored entities and the U.S. Treasury accounted for more than 91% of the total available-for-sale portfolio as of March 31, 2011 and no credit losses are expected, given the explicit and implicit guarantees provided by the U.S. federal government. The Corporation's assessment was concentrated mainly on private label mortgage-backed securities (MBS) of approximately \$95 million for which the Corporation evaluates credit losses on a quarterly basis. The Corporation considered the following factors in determining whether a credit loss exists and the period over which the debt security is expected to recover:

The length of time and the extent to which the fair value has been less than the amortized cost basis.

Changes in the near term prospects of the underlying collateral of a security such as changes in default rates, loss severity given default and significant changes in prepayment assumptions;

The level of cash flows generated from the underlying collateral supporting the principal and interest payments of the debt securities; and

Any adverse change to the credit conditions and liquidity of the issuer, taking into consideration the latest information available about the overall financial condition of the issuer, credit ratings, recent legislation and government actions affecting the issuer's industry and actions taken by the issuer to deal with the present economic climate.

No OTTI losses on available-for-sale debt securities were recorded during the quarters ended March 31, 2011 and 2010. Cumulative unrealized OTTI losses recognized in OCI as of March 31, 2011 amounted to \$27.1 million.

Private label MBS are collateralized by fixed-rate mortgages on single family residential properties in the United States. The interest rate on these private-label MBS is variable, tied to 3-month LIBOR and limited to the weighted-average coupon of the underlying collateral. The underlying mortgages are fixed-rate single family loans with original high FICO scores (over 700) and moderate original loan-to-value ratios (under 80%), as well as moderate delinquency levels.

Based on the expected cash flows derived from the model, and since the Corporation does not have the intention to sell the securities and has sufficient capital and liquidity to hold these securities until a recovery of the fair value occurs, no credit losses were reflected in earnings for the quarters ended March 31, 2011 and 2010. Significant assumptions in the valuation of the private label MBS as of March 31, 2011 and December 31, 2010 were as follow:

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	March 31, 2011		December 31, 2010	
	Weighted Average	Range	Weighted Average	Range
Discount rate	14.5%	14.5%	14.5%	14.5%
Prepayment rate	18%	13.56% - 26.82%	24%	18.2% - 43.73%
Projected Cumulative Loss Rate	5%	1.53% - 10.77%	6%	1.49% - 16.25%

For of the quarter ended on March 31, 2010, the Corporation recorded OTTI of approximately \$0.4 million on certain equity securities held in its available-for-sale investment portfolio related to financial institutions in Puerto Rico. No OTTI losses were recognized for the first quarter of 2011. Management concluded that the declines in value of the securities were other-than-temporary; as such, the cost basis of these securities was written down to the market value as of the date of the analysis and is reflected in earnings as a realized loss.

Total proceeds from the sale of securities available for sale during the quarter ended March 31, 2011 amounted to approximately \$41.4 million (2010 \$393.4 million excluding unsettled proceeds of \$57.1 million of securities sold).

5 OTHER EQUITY SECURITIES

Institutions that are members of the FHLB system are required to maintain a minimum investment in FHLB stock. Such minimum is calculated as a percentage of aggregate outstanding mortgages, and an additional investment is required that is calculated as a percentage of total FHLB advances, letters of credit, and the collateralized portion of interest-rate swaps outstanding. The stock is capital stock issued at \$100 par value. Both stock and cash dividends may be received on FHLB stock.

As of March 31, 2011 and December 31, 2010, the Corporation had investments in FHLB stock with a book value of \$50.1 million and \$54.6 million, respectively. The net realizable value is a reasonable proxy for the fair value of these instruments. Dividend income from FHLB stock for the quarters ended March 31, 2011 and 2010 amounted to \$0.7 million and \$0.8 million, respectively.

The FHLB stocks owned by the Corporation are issued by the FHLB of New York and by the FHLB of Atlanta. Both Banks are part of the Federal Home Loan Bank System, a national wholesale banking network of 12 regional, stockholder-owned congressionally chartered banks. The Federal Home Loan Banks are all privately capitalized and operated by their member stockholders. The system is supervised by the Federal Housing Finance Agency, which ensures that the Home Loan Banks operate in a financially safe and sound manner, remain adequately capitalized and able to raise funds in the capital markets, and carry out their housing finance mission.

The Corporation has other equity securities that do not have a readily available fair value. The carrying value of such securities as of March 31, 2011 and December 31, 2010 was \$1.3 million. An impairment charge of \$0.25 million was recorded in the first quarter of 2010 related to an investment in a failed financial institution in the United States. During the first quarter of 2010, the Corporation recognized a \$10.7 million gain on the sale of VISA Class C shares. The Corporation no longer holds any VISA shares.

During the first quarter of 2011, the Corporation completed the sale of loans with a book value of \$269.3 million to a new joint venture in exchange for \$88.5 million of cash, a \$136.1 million acquisition loan and a \$47.6 million, or 35%, equity interest in the new joint venture. The Corporation recorded the investment in the new joint venture using the equity method of accounting. Accordingly, the Corporation recorded the investment in the new joint venture at its transaction date fair value of \$47.6 million and included the investment as part of Other Equity Securities in the Statement of Financial Condition. Subsequently, the Corporation will recognize its share of earnings and losses of the new joint venture in the period in which the earnings or losses are recorded.

Table of Contents**6 LOANS RECEIVABLE**

The following is a detail of the loan portfolio held for investment:

	March 31, 2011	December 31, 2010
	(In thousands)	
Residential mortgage loans, mainly secured by first mortgages	\$ 2,896,692	\$ 3,417,417
Commercial loans:		
Construction loans	682,245	700,579
Commercial mortgage loans	1,588,768	1,670,161
Commercial and Industrial loans ⁽¹⁾	3,977,301	3,861,545
Loans to local financial institutions collateralized by real estate mortgages	285,359	290,219
Commercial loans	6,533,673	6,522,504
Finance leases	272,392	282,904
Consumer loans	1,387,018	1,432,611
Loans receivable	11,089,775	11,655,436
Allowance for loan and lease losses	(561,695)	(553,025)
Loans receivable, net	\$ 10,528,080	\$ 11,102,411

1 - As of March 31, 2011, includes \$1.7 billion of commercial loans that are secured by real estate but are not dependent upon the real estate for repayment.

Loans held for investment on which accrual of interest income had been discontinued as of March 31, 2011 and December 31, 2010 were as follows:

	March 31, 2011	December 31, 2010
<i>(Dollars in thousands)</i>		
Non-performing loans:		
Residential mortgage	\$ 391,962	\$ 392,134
Commercial mortgage	129,828	217,165
Commercial and Industrial	327,477	317,243
Construction	341,179	263,056
Consumer:		
Auto loans	19,987	25,350
Finance leases	3,632	3,935
Other consumer loans	18,986	20,106

Total non-performing loans held for investment ⁽¹⁾	\$ 1,233,051	\$ 1,238,989
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1 - As of March 31, 2011 and December 31, 2010, excludes \$5.5 million and \$159.3 million, respectively, in non-performing loans held for sale.

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The Corporation's aging of the loans held for investment portfolio as of March 31, 2011, follows:

As of March 31, 2011	Current	30-89 days Past Due	90 days or more Past Due ⁽¹⁾ (in thousands)	Total Portfolio	90 days and still accruing
Residential Mortgage:					
FHA/VA and other government guaranteed loans ⁽²⁾	\$ 142,570	\$ 16,582	\$ 84,425	\$ 243,577	\$ 84,425
Other residential mortgage loans	2,144,706	104,008	404,401	2,653,115	12,439
Commercial:					
Commercial & Industrial Loans	3,811,285	81,032	370,343	4,262,660	42,866
Commercial Mortgage Loans	1,360,791	93,459	134,518	1,588,768	4,690
Construction Loans	315,823	15,364	351,058	682,245	9,879
Consumer:					
Auto	869,931	93,250	19,987	983,168	
Finance Leases	250,171	18,589	3,632	272,392	
Other Consumer Loans	364,426	20,438	18,986	403,850	
Total Loans Receivable	\$ 9,259,703	\$ 442,722	\$ 1,387,350	\$ 11,089,775	\$ 154,299

- (1) Includes non-performing loans and accruing loans which are contractually delinquent 90 days or more (i.e. FHA/VA and other guaranteed loans).
- (2) As of March 31, 2011, includes \$58.1 million of defaulted loans collateralizing Ginnie Mae (GNMA) securities for which the Corporation has an unconditional option (but not an obligation) to repurchase the defaulted loans.

The Corporation's primary lending area is Puerto Rico. The Corporation's Puerto Rico banking subsidiary, FirstBank, also lends in the U.S. and British Virgin Islands markets and in the United States (principally in the state of Florida). Of the total gross loans held for investment portfolio of \$11.1 billion as of March 31, 2011, approximately 83% have credit risk concentration in Puerto Rico, 8% in the United States and 9% in the Virgin Islands.

As of March 31, 2011, the Corporation had \$325.9 million outstanding of credit facilities granted to the Puerto Rico Government and/or its political subdivisions, up from \$325.1 million as of December 31, 2010, and \$98.8 million granted to the Virgin Islands government, up from \$84.3 million as of December 31, 2010. A substantial portion of these credit facilities are obligations that have a specific source of income or revenues identified for their repayment, such as property taxes collected by the central Government and/or municipalities. Another portion of these obligations consists of loans to public corporations that obtain revenues from rates charged for services or products, such as electric power and water utilities. Public corporations have varying degrees of independence from the central Government and many receive appropriations or other payments from it. The Corporation also has loans to various municipalities in Puerto Rico for which the good faith, credit and unlimited taxing power of the applicable municipality have been pledged to their repayment.

Aside from loans extended to the Puerto Rico Government and its political subdivision, the largest loan to one borrower as of March 31, 2011 in the amount of \$285.4 million is with one mortgage originator in Puerto Rico, Doral Financial Corporation. This commercial loan is secured by individual real-estate loans, mostly 1-4 residential mortgage loans.

7 ALLOWANCE FOR LOAN AND LEASE LOSSES AND IMPAIRED LOANS

The changes in the allowance for loan and lease losses for the period ended March 31, 2011 were as follows:

(Dollars in thousands)	Residential Mortgage Loans	Commercial Mortgage Loans	Commercial & Industrial Loans	Construction Loans	Consumer Loans	Total
March 31, 2011						
Allowance for loan and lease losses:						
Beginning balance	\$ 62,330	\$ 105,596	\$ 152,641	\$ 151,972	\$ 80,486	\$ 553,025
Charge-offs	(5,404)	(31,171)	(16,344)	(19,165)	(11,969)	(84,053)
Recoveries	243	67	56	1,927	1,698	3,991
Provision	6,327	13,381	41,486	22,463	5,075	88,732
Ending balance	\$ 63,496	\$ 87,873	\$ 177,839	\$ 157,197	\$ 75,290	\$ 561,695
Ending balance: specific reserve for impaired loans	\$ 43,295	\$ 29,610	\$ 81,989	\$ 98,167	\$ 415	\$ 253,476
Ending balance: general allowance	\$ 20,201	\$ 58,263	\$ 95,850	\$ 59,030	\$ 74,875	\$ 308,219
Loans receivables:						
Ending balance	\$ 2,896,692	\$ 1,588,768	\$ 4,262,660	\$ 682,245	\$ 1,659,410	\$ 11,089,775
Ending balance: impaired loans	\$ 566,270	\$ 232,054	\$ 395,979	\$ 365,412	\$ 2,407	\$ 1,562,122
Ending balance: loans with general allowance	\$ 2,330,422	\$ 1,356,714	\$ 3,866,681	\$ 316,833	\$ 1,657,003	\$ 9,527,653

There were no significant purchases of loans during 2011. The Corporation did sell approximately \$236 million of performing residential mortgage loans to another financial institution and \$20.7 million of performing residential mortgage loans in the secondary market to FNMA and FHLMC during the first quarter of 2011. Also, the Corporation securitized approximately \$41.5 million of

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FHA/VA mortgage loan production to GNMA mortgage-backed securities during 2011. Refer to Note 8 Loans held for sale for additional information about loans sold and loans reclassified from held for investment to held for sale during the first quarter of 2011.

Changes in the allowance for the quarter ended March 31, 2010 were as follows:

	March 31, 2010
	(In thousands)
Balance at beginning of the period	\$ 528,120
Provision for loan and lease losses	170,965
Losses charged against the allowance	(126,306)
Recoveries credited to the allowance	2,524
Balance at end of period	\$ 575,303

The allowance for impaired loans is part of the allowance for loan and lease losses. The allowance for impaired loans covers those loans for which management has determined that it is probable that the debtor will be unable to pay all the amounts due in accordance with the contractual terms of the loan agreement, and does not necessarily represent loans for which the Corporation will incur a loss.

Information regarding impaired loans for the periods ended March 31, 2011 and December 31, 2010 was as follows:

Impaired Loans (Dollars in thousands) As of March 31, 2011 With no related allowance recorded:	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
FHA/VA Guaranteed loans	\$	\$	\$	\$	\$
Other residential mortgage loans	293,488	301,581		269,068	3,463
Commercial:					
Commercial mortgage loans	18,628	19,824		25,478	543
Commercial & Industrial Loans	63,328	73,342		58,980	225
Construction Loans	37,910	40,220		31,492	127
Consumer:					
Auto loans					
Finance leases					
Other consumer loans	1,141	1,496		901	6
	\$ 414,495	\$ 436,463	\$	\$ 385,919	\$ 4,364
With an allowance recorded:					
FHA/VA Guaranteed loans	\$	\$	\$	\$	\$
Other residential mortgage loans	272,782	309,570	43,295	291,984	1,307
Commercial:					
Commercial mortgage loans	213,426	268,508	29,610	181,934	2,051
Commercial & Industrial Loans	332,651	430,517	81,989	328,929	2,154
Construction Loans	327,502	433,556	98,167	282,737	1,478
Consumer:					

Auto loans					
Finance leases					
Other consumer loans	1,266	1,266	415	1,381	6
	\$ 1,147,627	\$ 1,443,417	\$ 253,476	\$ 1,086,965	\$ 6,996
Total:					
FHA/VA Guaranteed loans	\$	\$	\$	\$	\$
Other residential mortgage loans	566,270	611,151	43,295	561,052	4,770
Commercial:					
Commercial mortgage loans	232,054	288,332	29,610	207,412	2,594
Commercial & Industrial Loans	395,979	503,859	81,989	387,909	2,379
Construction Loans	365,412	473,776	98,167	314,229	1,605
Consumer:					
Auto loans					
Finance leases					
Other consumer loans	2,407	2,762	415	2,282	12
	\$ 1,562,122	\$ 1,879,880	\$ 253,476	\$ 1,472,884	\$ 11,360

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	Recorded Investment	Unpaid Principal Balance	Related Allowance
As of December 31, 2010			
With no related allowance recorded:			
FHA/VA Guaranteed loans	\$	\$	\$
Other residential mortgage loans	244,648	253,636	
Commercial:			
Commercial mortgage loans	32,328	32,868	
Commercial & Industrial Loans	54,631	58,927	
Construction Loans	25,074	26,557	
Consumer:			
Auto loans			
Finance leases			
Other consumer loans	659	1,015	
	\$ 357,340	\$ 373,003	\$
With an allowance recorded:			
FHA/VA Guaranteed loans	\$	\$	\$
Other residential mortgage loans	311,187	350,576	42,666
Commercial:			
Commercial mortgage loans	150,442	186,404	26,869
Commercial & Industrial Loans	325,206	416,919	65,030
Construction Loans	237,970	323,127	57,833
Consumer:			
Auto loans			
Finance leases			
Other consumer loans	1,496	1,496	264
	\$ 1,026,301	\$ 1,278,522	\$ 192,662
Total:			
FHA/VA Guaranteed loans	\$	\$	\$
Other residential mortgage loans	555,835	604,212	42,666
Commercial:			
Commercial mortgage loans	182,770	219,272	26,869
Commercial & Industrial Loans	379,837	475,846	65,030
Construction Loans	263,044	349,684	57,833
Consumer:			
Auto loans			
Finance leases			
Other consumer loans	2,155	2,511	264
	\$ 1,383,641	\$ 1,651,525	\$ 192,662

Interest income of approximately \$6.9 million was recognized on impaired loans for the quarter ended March 31, 2010. The average recorded investment in impaired loans for the first quarter of 2010 was \$1.7 billion.

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The following tables show the activity for impaired loans and the related specific reserve during the first quarter of 2011 and 2010:

	Quarter Ended	
	March 31, 2011	March 31, 2010
	(In thousands)	
Impaired Loans:		
Balance at beginning of period	\$ 1,383,641	\$ 1,656,264
Loans determined impaired during the period	277,548	317,333
Net charge-offs	(60,620)	(101,259)
Loans sold, net of charge-offs	(850)	(18,749)
Loans foreclosed, paid in full and partial payments or no longer considered impaired	(37,597)	(7,503)
Balance at end of period	\$ 1,562,122	\$ 1,846,086

	Quarter Ended	
	March 31, 2011	March 31, 2010
	(In thousands)	
Specific Reserve:		
Balance at beginning of period	\$ 192,662	\$ 182,145
Provision for loan losses	121,434	164,414
Net charge-offs	(60,620)	(101,259)
Balance at end of period	\$ 253,476	\$ 245,300

The Corporation's credit quality indicators by loan type as of March 31, 2011 and December 31, 2010 are summarized below:

	Commercial Credit Exposure-Credit risk Profile based on Creditworthiness category:	
	Adversely Classified⁽¹⁾	Total Portfolio
	(In thousands)	
March 31, 2011		
Commercial Mortgage	\$ 245,008	\$ 1,588,768
Construction	404,301	682,245
Commercial and Industrial	596,596	4,262,660
December 31, 2010		

Commercial Mortgage	\$ 353,860	\$ 1,670,161
Construction	323,880	700,579
Commercial and Industrial	558,937	4,151,764

(1) Excludes \$5.5 million (construction) as of March 31, 2011 and \$261.8 million as of December 31, 2010 (\$205.7 million construction; \$35.4 million commercial mortgage; \$20.7 million commercial and industrial) of adversely classified loans held for sale.

The Corporation considered a loan as adversely classified if its risk rating is Substandard, Doubtful or Loss. These categories are defined as follows:

Substandard- A Substandard Asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must 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- Doubtful classifications have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable. A Doubtful classification may be appropriate in cases where significant risk exposures are perceived, but Loss cannot be determined because of specific reasonable pending factors which may strengthen the credit in the near term.

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Loss- Assets classified 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 it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be affected in the future. There is little or no prospect for near term improvement and no realistic strengthening action of significance pending.

March 31, 2011	Consumer Credit Exposure-Credit risk Profile based on payment activity				
	Residential Real-Estate			Consumer	
	FHA/VA/Guaranteed	Other residential	Auto	Finance Leases	Other Consumer
		loans			
	(In thousands)				
Performing	\$ 243,577	\$ 2,261,153	\$ 963,181	\$ 268,760	\$ 384,864
Non-performing		391,962	19,987	3,632	18,986
Total	\$ 243,577	\$ 2,653,115	\$ 983,168	\$ 272,392	\$ 403,850

December 31, 2010	Consumer Credit Exposure-Credit risk Profile based on payment activity				
	Residential Real-Estate			Consumer	
	FHA/VA/Guaranteed	Other residential	Auto	Finance Leases	Other Consumer
		loans			
	(In thousands)				
Performing	\$ 232,522	\$ 2,792,761	\$ 983,626	\$ 278,969	\$ 403,529
Non-performing		392,134	25,350	3,935	20,106
Total	\$ 232,522	\$ 3,184,895	\$ 1,008,976	\$ 282,904	\$ 423,635

The Corporation provides homeownership preservation assistance to its customers through a loss mitigation program in Puerto Rico and through programs sponsored by the Federal Government. Depending upon the nature of borrowers' financial condition, restructurings or loan modifications through this program as well as other restructurings of individual commercial, commercial mortgage, construction and residential mortgage loans in the U.S. mainland fit the definition of TDR. A restructuring of a debt constitutes a TDR if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider. Modifications involve changes in one or more of the loan terms that bring a defaulted loan current and provide sustainable affordability. Changes may include the refinancing of any past-due amounts, including interest and escrow, the extension of the maturity of the loan and modifications of the loan rate. As of March 31, 2011, the Corporation's TDR loans consisted of \$291.2 million of residential mortgage loans, \$40.7 million commercial and industrial loans, \$139.9 million commercial mortgage loans and \$15.4 million of construction loans. Outstanding unfunded loan commitments on TDR loans amounted to \$1.2 million as of March 31, 2011.

Included in the \$139.9 million of commercial mortgage TDR loans are certain loan relationships restructured through loan splitting, one in the first quarter of 2011 and one in the fourth quarter of 2010. Each of these loan relationships were restructured into two notes; one that represents the portion of the loan that is expected to be fully collected along with contractual interest and the second note that represents the portion of the original loan that was charged-off. The renegotiations of these loans have been made after analyzing the borrowers' and guarantors' capacity to repay the debt and ability to perform under the modified terms. For the relationship restructured in the first quarter

of 2011, the first note of \$57.5 million was placed on a monthly payment that amortize the debt over 30 years at a market rate of interest. The second note, amounting to \$28.3 million was fully charged-off. For the relationship restructured in the fourth quarter of 2010, as part of the renegotiation of the loans, the first note of \$17 million was placed on a monthly payment schedule that amortizes the debt over 30 years at a market rate of interest. The second note for \$2.7 million was fully charged-off. The following tables provide additional information about the volume of this type of loan restructurings and the effect on the allowance for loan and lease losses in 2011.

Principal balance deemed collectible at end of period	\$ 74,442
Amount charged-off during the first quarter of 2011	\$ 28,340
 Allowance for loan losses:	
Balance at beginning of period	\$ 23,108
Provision for loan losses	7,205
Charge-offs	(28,340)
Balance at end of period	\$ 1,973

The loans comprising the \$74.4 million that have been deemed collectible were placed in accruing status as the borrowers have exhibited a period of sustained performance but continue to be individually evaluated for impairment purposes. These transactions contributed to a \$105.3 million decrease in non-performing loans over the last two quarters.

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As of March 31, 2011, the Corporation maintains a \$5.5 million reserve for unfunded loan commitments mainly related to outstanding construction loans commitments. The reserve for unfunded loan commitments is an estimate of the losses inherent in off-balance sheet loan commitments at the balance sheet date. It is calculated by multiplying an estimated loss factor by an estimated probability of funding, and then by the period-end amounts for unfunded commitments. The reserve for unfunded loan commitments is included as part of accounts payable and other liabilities in the consolidated statement of financial condition.

8 LOANS HELD FOR SALE

As of March 31, 2011 and December 31, 2010, the Corporation's loans held for sale portfolio was composed of:

	March 31, 2011	December 31, 2010
	(In thousands)	
Residential mortgage loans	\$ 299,441	\$ 19,148
Construction loans	6,053	207,270
Commercial and Industrial loans		20,643
Commercial mortgage loans		53,705
Total	\$ 305,494	\$ 300,766

During the first quarter of 2011, the Corporation reclassified approximately \$282 million of loans, mainly residential mortgage loans, from held for investment to held for sale pursuant to a letter of intent to sell loans entered into by FirstBank with another financial institution. The loans were subsequently sold in April 2011.

Non-performing loans held for sale totaled \$5.5 million (construction) and \$159.3 million (\$140.1 million construction loans and \$19.2 million commercial mortgage loans) as of March 31, 2011 and December 31, 2010, respectively.

At the end of the fourth quarter of 2010, the Corporation transferred \$447 million of loans to held for sale at a value of \$281.6 million. This resulted in charge-offs at the time of transfer of \$165.1 million. During the first quarter of 2011, these loans with a book value of \$269.3 million were sold to a new joint venture created by Goldman, Sachs & Co. and Caribbean Property Group in exchange for \$88.5 million of cash, an acquisition loan of \$136.1 million and a \$47.6 million, or 35%, interest in the joint venture. At March 31, 2011, the only related balance remaining from loans transferred in the fourth quarter of 2010 amounted to \$5.5 million. Further details of this transaction are discussed in Note 11.

9 DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

One of the market risks facing the Corporation is interest rate risk, which includes the risk that changes in interest rates will result in changes in the value of the Corporation's assets or liabilities and the risk that net interest income from its loan and investment portfolios will be adversely affected by changes in interest rates. The overall objective of the Corporation's interest rate risk management activities is to reduce the variability of earnings caused by changes in interest rates.

The Corporation designates a derivative as a fair value hedge, cash flow hedge or as an economic undesignated hedge when it enters into the derivative contract. As of March 31, 2011 and December 31, 2010, all derivatives held by the Corporation were considered economic undesignated hedges. These undesignated hedges are recorded at fair value with the resulting gain or loss recognized in current earnings.

The following summarizes the principal derivative activities used by the Corporation in managing interest rate risk: Interest rate cap agreements Interest rate cap agreements provide the right to receive cash if a reference interest rate rises above a contractual rate. The value increases as the reference interest rate rises. The Corporation enters into interest rate cap agreements for protection from rising interest rates. Specifically, the interest rate on certain of the Corporation's commercial loans to other financial institutions is generally a variable rate limited to the weighted-average coupon of the referenced residential mortgage collateral, less a contractual servicing fee. During the

second quarter of 2010, the counterparty for interest rate caps for certain private label MBS was taken over by the FDIC, which resulted in the immediate cancelation of all outstanding commitments, and

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as a result, interest rate caps with a notional amount of \$103 million are no longer considered to be derivative financial instruments. The total exposure to fair value of \$3.0 million related to such contracts was reclassified to an account receivable.

Interest rate swaps Interest rate swap agreements generally involve the exchange of fixed and floating-rate interest payment obligations without the exchange of the underlying notional principal amount. As of March 31, 2011, most of the interest rate swaps outstanding are used for protection against rising interest rates. Similar to unrealized gains and losses arising from changes in fair value, net interest settlements on interest rate swaps are recorded as an adjustment to interest income or interest expense depending on whether an asset or liability is being economically hedged.

Indexed options Indexed options are generally over-the-counter (OTC) contracts that the Corporation enters into in order to receive the appreciation of a specified Stock Index (e.g., Dow Jones Industrial Composite Stock Index) over a specified period in exchange for a premium paid at the contract's inception. The option period is determined by the contractual maturity of the notes payable tied to the performance of the Stock Index. The credit risk inherent in these options is the risk that the exchange party may not fulfill its obligation.

Forward Contracts Forward contracts are sales of to-be-announced (TBA) mortgage-backed securities that will settle over the standard delivery date and do not qualify as regular way security trades. Regular-way security trades are contracts with no net settlement provision and no market mechanism to facilitate net settlement and they provide for delivery of a security within the time generally established by regulations or conventions in the market-place or exchange in which the transaction is being executed. The forward sales are considered derivative instruments that need to be marked-to-market. These securities are used to hedge the loan production of GNMA securities of the mortgage-banking operations. Unrealized gains (losses) are recognized as part of mortgage banking activities in the Consolidated Statement of (Loss) Income.

To satisfy the needs of its customers, the Corporation may enter into non-hedging transactions. On these transactions, generally, the Corporation participates as a buyer in one of the agreements and as a seller in the other agreement under the same terms and conditions.

In addition, the Corporation enters into certain contracts with embedded derivatives that do not require separate accounting as these are clearly and closely related to the economic characteristics of the host contract. When the embedded derivative possesses economic characteristics that are not clearly and closely related to the economic characteristics of the host contract, it is bifurcated, carried at fair value, and designated as a trading or non-hedging derivative instrument.

The following table summarizes the notional amounts of all derivative instruments as of March 31, 2011 and December 31, 2010:

	Notional Amounts	
	As of March 31, 2011	As of December 31, 2010
	(In thousands)	
Economic undesignated hedges:		
Interest rate contracts:		
Interest rate swap agreements used to hedge loans	\$ 40,860	\$ 41,248
Written interest rate cap agreements	71,364	71,602
Purchased interest rate cap agreements	71,364	71,602
Equity contracts:		
Embedded written options on stock index deposits and notes payable	53,515	53,515
Purchased options used to manage exposure to the stock market on embedded stock index options	53,515	53,515

Forward contracts:

Sales of TBA GNMA MBS pools

27,000

\$ 317,618

\$

291,482

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The following table summarizes the fair value of derivative instruments and the location in the Statement of Financial Condition as of March 31, 2011 and December 31, 2010:

	Asset Derivatives			Liability Derivatives		
	Statement of Financial Condition Location	March 31, 2011 Fair Value	December 31, 2010 Fair Value (In thousands)	Statement of Financial Condition Location	March 31, 2011 Fair Value	December 31, 2010 Fair Value
Economic undesignated hedges:						
Interest rate contracts:						
Interest rate swap agreements used to hedge loans	Other assets	\$ 316	\$ 351	Accounts payable and other liabilities	\$ 4,813	\$ 5,192
Written interest rate cap agreements	Other assets			Accounts payable and other liabilities	1	1
Purchased interest rate cap agreements	Other assets	1	1	Accounts payable and other liabilities		
Equity contracts:						
Embedded written options on stock index deposits	Other assets			Interest-bearing deposits		
Embedded written options on stock index notes payable	Other assets			Notes payable	2,167	1,508
Purchased options used to manage exposure to the stock market on embedded stock index options	Other assets	2,207	1,553	Accounts payable and other liabilities		
Forward Contracts:						
Sales of TBA GNMA MBS pools	Other assets	32		Accounts payable and other liabilities	296	
		\$ 2,556	\$ 1,905		\$ 7,276	\$ 6,701

The following table summarizes the effect of derivative instruments on the Statement of Loss for the quarters ended March 31, 2011 and March 31, 2010:

Location of Gain or (Loss) Recognized in Income on Derivatives	Unrealized Gain (Loss) Quarter Ended March 31,	
	2011	2010

(In thousands)

ECONOMIC UNDESIGNATED HEDGES:

Interest rate contracts:

Interest rate swap agreements used to hedge
fixed-rate:

Loans	Interest income - Loans	\$ 345	\$ (13)
Written and purchased interest rate cap agreements			
- mortgage-backed securities	Interest income - Investment securities		(697)
Written and purchased interest rate cap agreements			
- loans	Interest income - loans		(34)
Equity contracts:			
Embedded written and purchased options on stock index deposits	Interest expense - Deposits		(1)
Embedded written and purchased options on stock index notes payable	Interest expense - Notes payable and other borrowings	(5)	(30)
Forward contracts:			
Sales of TBA GNMA MBS pools	Mortgage Banking Activities	(264)	
Total gain (loss) on derivatives		\$ 76	\$ (775)

Derivative instruments, such as interest rate swaps, are subject to market risk. As is the case with investment securities, the market value of derivative instruments 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.

A summary of interest rate swaps as of March 31, 2011 and December 31, 2010 follows:

	As of March 31, 2011 (Dollars in thousands)	As of December 31, 2010
Pay fixed/receive floating :		
Notional amount	\$40,860	\$ 41,248
Weighted-average receive rate at period end	2.13%	2.14%
Weighted-average pay rate at period end	6.83%	6.83%
Floating rates range from 167 to 252 basis points over 3-month LIBOR		

As of March 31, 2011, the Corporation has not entered into any derivative instrument containing credit-risk-related contingent features.

Table of Contents**10 GOODWILL AND OTHER INTANGIBLES**

Goodwill as of March 31, 2011 and December 31, 2010 amounted to \$28.1 million, recognized as part of Other Assets. The Corporation conducted its annual evaluation of goodwill and intangibles during the fourth quarter of 2010. The evaluation was a two step process. The Step 1 evaluation of goodwill allocated to the Florida reporting unit indicated potential impairment of goodwill. The Step 1 fair value for the unit was below the carrying amount of its equity book value as of the October 1, 2010 valuation date, requiring the completion of Step 2. The Step 2 required a valuation of all assets and liabilities of the Florida unit, including any recognized and unrecognized intangible assets, to determine the fair value of net assets. To complete Step 2, the Corporation subtracted from the unit's Step 1 fair value the determined fair value of the net assets to arrive at the implied fair value of goodwill. The results of the Step 2 analysis indicated that the implied fair value of goodwill exceeded the goodwill carrying value by \$12.3 million, resulting in no goodwill impairment. Goodwill was not impaired as of December 31, 2010, nor was any goodwill written-off due to impairment during 2010. There have been no events related to the Florida reporting unit that could indicate potential goodwill impairment since the date of the last evaluation; therefore, no goodwill impairment evaluation was performed during the first quarter of 2011. Goodwill and other indefinite life intangibles are reviewed at least annually for impairment.

As of March 31, 2011, the gross carrying amount and accumulated amortization of core deposit intangibles was \$41.8 million and \$28.4 million, respectively, recognized as part of Other Assets in the consolidated statements of financial condition (December 31, 2010 \$41.8 million and \$27.8 million, respectively). For the quarter ended March 31, 2011, the amortization expense of core deposit intangibles amounted to \$0.6 million (2010 \$0.7 million).

11 VARIABLE INTEREST ENTITIES AND SERVICING ASSETS

The Corporation transfers residential mortgage loans in sale or securitization transactions in which it has continuing involvement, including servicing responsibilities and guarantee arrangements. All such transfers have been accounted for as sales as required by applicable accounting guidance.

When evaluating transfers and other transactions with Variable Interest Entities (VIEs) for consolidation under the recently adopted guidance, the Corporation first determines if the counterparty is an entity for which a variable interest exists. If no scope exception is applicable and a variable interest exists, the Corporation then evaluates if it is the primary beneficiary of the VIE and whether the entity should be consolidated or not.

Below is a summary of transfers of financial assets to VIEs for which the Corporation has retained some level of continuing involvement:

Ginnie Mae

The Corporation typically transfers first lien residential mortgage loans in conjunction with Ginnie Mae securitization transactions whereby the loans are exchanged for cash or securities that are readily redeemed for cash proceeds and servicing rights. The securities issued through these transactions are guaranteed by the issuer and, as such, under seller/servicer agreements the Corporation is required to service the loans in accordance with the issuers servicing guidelines and standards. As of March 31, 2011, the Corporation serviced loans securitized through GNMA with principal balance of \$502.6 million.

Trust Preferred Securities

In 2004, FBP Statutory Trust I, a financing subsidiary of the Corporation, sold to institutional investors \$100 million of its variable rate trust preferred securities. The proceeds of the issuance, together with the proceeds of the purchase by the Corporation of \$3.1 million of FBP Statutory Trust I variable rate common securities, were used by FBP Statutory Trust I to purchase \$103.1 million aggregate principal amount of the Corporation's Junior Subordinated Deferrable Debentures. Also in 2004, FBP Statutory Trust II, a statutory trust that is wholly-owned by the Corporation, sold to institutional investors \$125 million of its variable rate trust preferred securities. The proceeds of the issuance, together with the proceeds of the purchase by the Corporation of \$3.9 million of FBP Statutory Trust II variable rate common securities, were used by FBP Statutory Trust II to purchase \$128.9 million aggregate principal amount of the Corporation's Junior Subordinated Deferrable Debentures. The trust preferred debentures are presented in the Corporation's Consolidated Statement of Financial Condition as Other Borrowings, net of related issuance costs. The variable rate trust preferred securities are fully and unconditionally guaranteed by the Corporation. The \$100 million Junior Subordinated Deferrable Debentures issued by the Corporation in April 2004 and the

\$125 million issued in September 2004 mature on September 17, 2034 and September 20, 2034, respectively; however, under certain circumstances, the maturity of Junior Subordinated Debentures may be shortened (such shortening would result in a mandatory redemption of the variable rate trust preferred securities). The trust preferred securities, subject to certain limitations, qualify as Tier I regulatory capital under current Federal Reserve rules and regulations. The Collins Amendment to the Dodd-Frank Wall Street Reform and Consumer Protection Act eliminates certain trust preferred securities from Tier 1 Capital, but TARP preferred securities are exempted from this treatment. These regulatory capital deductions for trust preferred securities are to be phased in incrementally over a period of 3 years beginning on January 1, 2013.

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During 2004 and 2005, a third party to the Corporation, from now on identified as the seller, established a series of statutory trusts to effect the securitization of mortgage loans and the sale of trust certificates. The seller initially provided the servicing for a fee, which is senior to the obligations to pay trust certificate holders. The seller then entered into a sales agreement through which it sold and issued the trust certificates in favor of the Corporation's banking subsidiary. Currently, the Bank is the sole owner of the trust certificates; the servicing of the underlying residential mortgages that generate the principal and interest cash flows, is performed by another third party, which receives a fee compensation for services provided, the servicing fee. The securities are variable rate securities indexed to 90 day LIBOR plus a spread. The principal payments from the underlying loans are remitted to a paying agent (servicer) who then remits interest to the Bank; interest income is shared to a certain extent with the FDIC, that has an interest only strip (IO) tied to the cash flows of the underlying loans, whereas it is entitled to receive the excess of the interest income less a servicing fee over the variable rate income that the Bank earns on the securities. This IO is limited to the weighted average coupon of the securities. The FDIC became the owner of the IO upon the intervention of the seller, a failed financial institution. No recourse agreement exists and the risk from losses on non accruing loans and repossessed collateral are absorbed by the Bank as the sole holder of the certificates. As of March 31, 2011, the outstanding balance of Grantor Trusts amounted to \$95 million with a weighted average yield of 2.04%.

Joint Venture

On February 16, 2011, the Corporation sold an asset portfolio consisting of performing and non-performing construction, commercial mortgage and C&I loans with an aggregate book value of \$269.3 million to a new joint venture (the Joint Venture) organized under the Laws of the Commonwealth of Puerto Rico and majority owned by PRLP Ventures LLC (PRLP), a company created by Goldman, Sachs & Co. and Caribbean Property Group (CPG). In exchange for the sale, the Corporation received \$88.5 million in cash; a 35% interest in the Joint Venture, valued at \$47.6 million; and \$136.1 million representing seller financing provided by FirstBank, which has a 7-year maturity and bears variable interest at 30-day LIBOR plus 300 basis points and is secured by a pledge of all of the acquiring entity's assets as well as the PRLP's 65% ownership interest in the Joint Venture. As of March 31, 2011, the carrying amount of the loan is \$136.1 million and is included in the Corporation's C&I loan receivable portfolio; while the carrying value of FirstBank's equity interest is \$47.6 million as of March 31, 2011 and is included as part of Other Equity Securities in the Statement of Financial Condition.

FirstBank will additionally provide an \$80 million advance facility to the Joint Venture to fund unfunded commitments and costs to complete projects under construction, of which \$45.7 million were disbursed in the first quarter of 2011, and a \$20 million working capital line of credit to fund certain expenses of the Joint Venture. These loans will bear variable interest at 30-day LIBOR plus 300 basis points. As of March 31, 2011, the carrying value of the advance facility and working capital line were \$45.7 million and \$0, respectively, and are included in the Corporation's C&I loan receivable portfolio.

The Corporation has determined that the Joint Venture is a VIE in which the Corporation is not the primary beneficiary. In determining the primary beneficiary of the Joint Venture, the Corporation considered applicable guidance which requires the Corporation to qualitatively assess the determination of the primary beneficiary (or consolidator) of the Joint Venture on whether it has both the power to direct the activities of the Joint Venture that most significantly impact the entity's economic performance; and the obligation to absorb losses of the Joint Venture that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. The Corporation determined that it does not have the power to direct the activities that most significantly impact the economic performance of the Joint Venture as it does not have the right to manage the loan portfolio, impact foreclosure proceedings, or manage the construction and sale of the property; therefore, the Corporation concluded that it is not the primary beneficiary of the Joint Venture. As a creditor to the Joint Venture, the Corporation has certain rights related to the Joint Venture, however, these are intended to be protective in nature and do not provide the Corporation with the ability to manage the operations of the Joint Venture. Because the Joint Venture is not a consolidated subsidiary of the Corporation, the Corporation accounted for this transaction as a true sale, recognizing in books the cash received, the notes receivable and the interest in the joint venture and derecognizing the loan portfolio sold.

Servicing Assets

The Corporation is actively involved in the securitization of pools of FHA-insured and VA-guaranteed mortgages for issuance of GNMA mortgage-backed securities. Also, certain conventional conforming-loans are sold to FNMA or FHLMC with servicing retained. The Corporation recognizes as separate assets the rights to service loans for others, whether those servicing assets are originated or purchased.

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The changes in servicing assets are shown below:

	March 31, 2011	March 31, 2010
	(In thousands)	
Balance at beginning of period	\$ 15,597	\$ 11,902
Capitalization of servicing assets	1,231	1,686
Amortization	(524)	(435)
Adjustment to servicing assets for loans repurchased (1)	(61)	(559)
Balance before valuation allowance at end of period	16,243	12,594
Valuation allowance for temporary impairment	(1,237)	(180)
Balance at end of period	\$ 15,006	\$ 12,414

(1) Amount represents the adjustment to fair value related to the repurchase in the quarters ended March 31, 2011 and 2010 of \$12.0 million and \$53.5 million, respectively, in principal balance of loans serviced for others. Impairment charges are recognized through a valuation allowance for each individual stratum of servicing assets. The valuation allowance is adjusted to reflect the amount, if any, by which the cost basis of the servicing asset for a given stratum of loans being serviced exceeds its fair value. Any fair value in excess of the cost basis of the servicing asset for a given stratum is not recognized. Other-than-temporary impairments, if any, are recognized as a direct write-down of the servicing assets.

Changes in the impairment allowance were as follows:

	March 31, 2011	March 31, 2010
	(In thousands)	
Balance at beginning of period	\$ 434	\$ 745
Temporary impairment charges	974	136
Recoveries	(171)	(701)
Balance at end of period	\$ 1,237	\$ 180

The components of net servicing income are shown below:

	March 31, 2011	March 31, 2010
	(In thousands)	
Servicing fees	\$ 1,251	\$ 928
Late charges and prepayment penalties	244	114
Other (1)	(61)	(559)
Servicing income, gross	1,434	483
(Amortization and impairment) recovery of servicing assets	(1,327)	130

Servicing income, net	\$ 107	\$ 613
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(1) Amount represents the adjustment to fair value related to the repurchase in the quarters ended March 31, 2011 and 2010 of \$12.0 million and \$53.5 million, respectively, in principal balance of loans serviced for others.

The Corporation's servicing assets are subject to prepayment and interest rate risks. Constant prepayment rate assumptions for the Corporation's servicing assets for the quarter ended March 31, 2011 and the quarter ended March 31, 2010 were 10.6% and 12.7% for government guaranteed mortgage loans, respectively. For conventional conforming mortgage loans, the Corporation used 12.7% and 14.8% and for conventional non-conforming mortgage loans 11.7% and 11.5% for the periods ended March 31, 2011 and March 31, 2010, respectively. Discount rate assumptions used were 11.3% and 10.3% for government guaranteed mortgage loans; 9.3% for conventional conforming mortgage loans; and 15.0% and 13.1% for conventional non-conforming mortgage loans for the periods ended March 31, 2011 and March 31, 2010, respectively.

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At March 31, 2011, fair values of the Corporation's servicing assets were based on a valuation model that incorporates market driven assumptions, adjusted by the particular characteristics of the Corporation's servicing portfolio, regarding discount rates and mortgage prepayment rates. The weighted-averages of the key economic assumptions used by the Corporation in its valuation model and the sensitivity of the current fair value to immediate 10 percent and 20 percent adverse changes in those assumptions for mortgage loans at March 31, 2011, were as follows:

	(Dollars in thousands)
Carrying amount of servicing assets	\$ 15,006
Fair value	\$ 15,719
Weighted-average expected life (in years)	8.5
Constant prepayment rate (weighted-average annual rate)	11.74%
Decrease in fair value due to 10% adverse change	\$ 707
Decrease in fair value due to 20% adverse change	\$ 1,368
Discount rate (weighted-average annual rate)	10.42%
Decrease in fair value due to 10% adverse change	\$ 614
Decrease in fair value due to 20% adverse change	\$ 1,186

These sensitivities are hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a 10 percent variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the servicing asset is calculated without changing any other assumption; in reality, 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 counteract the sensitivities.

12 DEPOSITS

The following table summarizes deposit balances:

	March 31, 2011	December 31, 2010
	(In thousands)	
Type of account:		
Non-interest bearing checking accounts	\$ 707,938	\$ 668,052
Savings accounts	1,968,350	1,938,475
Interest-bearing checking accounts	1,055,648	1,012,009
Certificates of deposit	2,263,273	2,181,205
Brokered certificates of deposit	5,721,227	6,259,369
	\$ 11,716,436	\$ 12,059,110

The following are the components of interest expense on deposits:

	Quarter Ended	
	March 31, 2011	March 31, 2010
	(In thousands)	
Interest expense on deposits	\$ 48,700	\$ 60,500

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Amortization of broker placement fees	5,359	5,465
Interest expense on deposits excluding net unrealized loss (gain) on derivatives and brokered CDs measured at fair value	54,059	65,965
Net unrealized loss on derivatives		1
Total interest expense on deposits	\$ 54,059	\$ 65,966

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Securities sold under agreements to repurchase (repurchase agreements) consist of the following:

	March 31, 2011	December 31, 2010
	(In thousands)	
Repurchase agreements, interest ranging from 0.99% to 4.51%	\$ 1,400,000	\$ 1,400,000

Repurchase agreements mature as follows:

	March 31, 2011
	(In thousands)
Over ninety days to one year	\$ 100,000
One to three years	700,000
Three to five years	600,000
Total	\$ 1,400,000

As of March 31, 2011 and December 31, 2010, the securities underlying such agreements were delivered to the dealers with whom the repurchase agreements were transacted.

Repurchase agreements as of March 31, 2011, grouped by counterparty, were as follows:

Counterparty	Amount	Weighted-Average Maturity (In Months)
UBS Financial Services, Inc.	\$ 100,000	16
Barclays Capital	200,000	17
Credit Suisse First Boston	400,000	27
Dean Witter / Morgan Stanley	200,000	28
JP Morgan Chase	200,000	36
Citigroup Global Markets	300,000	37
	\$ 1,400,000	

14 ADVANCES FROM THE FEDERAL HOME LOAN BANK (FHLB)

Following is a summary of the advances from the FHLB:

	March 31, 2011	December 31, 2010
	(In thousands)	
Fixed-rate advances from FHLB, with a weighted-average interest rate of 3.32% (2010 - 3.33%)	\$ 540,440	\$ 653,440

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Advances from FHLB mature as follows:

	March 31, 2011 (In thousands)
One to thirty days	\$ 5,000
Over thirty to ninety days	15,000
Over ninety days to one year	167,000
One to three years	353,440
Total	\$ 540,440

As of March 31, 2011, the Corporation had additional capacity of approximately \$486.4 million on this credit facility based on collateral pledged at the FHLB, including haircuts reflecting the perceived risk associated with holding the collateral.

15 NOTES PAYABLE

Notes payable consist of:

	March 31, 2011	December 31, 2010
	(Dollars in thousands)	
Callable step-rate notes, bearing step increasing interest from 5.00% to 7.00% (6.00% as of March 31, 2011 and December 31, 2010) maturing on October 18, 2019, measured at fair value	\$ 12,437	\$ 11,842
Dow Jones Industrial Average (DJIA) linked principal protected notes:		
Series A maturing on February 28, 2012	7,175	6,865
Series B maturing on May 27, 2011	8,225	7,742
	\$ 27,837	\$ 26,449

16 OTHER BORROWINGS

Other borrowings consist of:

	March 31, 2011	December 31, 2010
	(Dollars in thousands)	
Junior subordinated debentures due in 2034, interest-bearing at a floating-rate of 2.75% over 3-month LIBOR (3.06% as of March 31, 2011 and 3.05% as of December 31, 2010)	\$ 103,093	\$ 103,093
Junior subordinated debentures due in 2034, interest-bearing at a floating-rate of 2.50% over 3-month LIBOR (2.81% as of March 31, 2011 and 2.80% as of December 31, 2010)	128,866	128,866
	\$ 231,959	\$ 231,959

17 STOCKHOLDERS EQUITY

Common Stock

As of March 31, 2011, the Corporation had 2,000,000,000 authorized shares of common stock with a par value of \$0.10 per share. As of both March 31, 2011 and December 31, 2010, there were 21,963,522 shares issued and 21,303,669 shares outstanding. The Corporation stopped paying common and preferred stock dividends since August 2009.

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As of March 31, 2011, there were 716 shares of restricted stock outstanding that are expected to vest in the fourth quarter of 2011. The shares of restricted stock may vest more quickly in the event of death, disability, retirement, or a change in control. Based on particular circumstances evaluated by the Compensation Committee as they may relate to the termination of a restricted stock holder, the Corporation's Board of Directors may, with the recommendation of the Compensation Committee, grant the full vesting of the restricted stock held upon termination of employment. Holders of restricted stock have the right to dividends or dividend equivalents, as applicable, during the restriction period. Such dividends or dividend equivalents will accrue during the restriction period, but will not be paid until restrictions lapse. The holder of restricted stock has the right to vote the shares.

Effective January 7, 2011, the Corporation implemented a one-for-fifteen reverse stock split of all outstanding shares of its common stock. At the Corporation's Special Meeting of Stockholders held on August 24, 2010, stockholders approved an amendment to the Corporation's Restated Articles of Incorporation to implement a reverse stock split at a ratio, to be determined by the board in its sole discretion, within the range of one new share of common stock for 10 old shares and one new share for 20 old shares. As authorized, the board elected to effect a reverse stock split at a ratio of one-for-fifteen. The reverse stock split allowed the Corporation to regain compliance with listing standards of the New York Stock Exchange. The one-for-fifteen reverse stock split reduced the number of outstanding shares of common stock from 319,557,932 shares to 21,303,669 shares of common stock. All share and per share amounts included in these financial statements have been adjusted to retroactively reflect the 1-for-15 reverse stock split.

Preferred Stock

The Corporation has 50,000,000 authorized shares of preferred stock with a par value of \$1, redeemable at the Corporation's option subject to certain terms. This stock may be issued in series and the shares of each series shall have such rights and preferences as shall be fixed by the Board of Directors when authorizing the issuance of that particular series. As of March 31, 2011, the Corporation has five outstanding series of non-convertible non-cumulative preferred stock: 7.125% non-cumulative perpetual monthly income preferred stock, Series A; 8.35% non-cumulative perpetual monthly income preferred stock, Series B; 7.40% non-cumulative perpetual monthly income preferred stock, Series C; 7.25% non-cumulative perpetual monthly income preferred stock, Series D; and 7.00% non-cumulative perpetual monthly income preferred stock, Series E. The liquidation value per share is \$25. The Corporation is currently in the process of voluntarily delisting the Series A through E preferred stock from the New York Stock Exchange.

On July 20, 2010, the Corporation issued \$424.2 million Fixed Rate Cumulative Mandatorily Convertible Preferred Stock, Series G (the "Series G Preferred Stock"), in exchange of the \$400 million of Fixed Rate Cumulative Perpetual Preferred Stock, Series F (the "Series F Preferred Stock"), that the U.S. Treasury had acquired pursuant to the TARP Capital Purchase Program, and dividends accrued on such stock. A key benefit of this transaction was obtaining the right, under the terms of the new Series G Preferred Stock, to compel the conversion of this stock into shares of the Corporation's common stock, provided that the Corporation meets a number of conditions, and by the Treasury and any subsequent holder at any time and, unless earlier converted, is automatically convertible into common stock on the seventh anniversary of issuance. On the seventh anniversary of issuance, each share of the Series G Preferred Stock will mandatorily convert into a number of shares of the Corporation's common stock equal to a fraction, the numerator of which is \$1,000 and the denominator of which is the market price of the Corporation's common stock on the second trading day preceding the mandatory conversion date, provided, however, holders of the Series G Preferred Stock shall not be entitled to convert shares until the converting holder has first received any applicable regulatory approvals. On August 24, 2010, the Corporation obtained its stockholders' approval to increase the number of authorized shares of common stock from 750 million to 2 billion and decrease the par value of its common stock from \$1.00 to \$0.10 per share. These approvals and the issuance in 2010 of common stock in exchange for Series A through E preferred stock satisfy all but one of the substantive conditions to the Corporation's ability to compel the conversion of the 424,174 shares of the new series of Series G Preferred Stock, issued to the U.S. Treasury. The other substantive condition to the Corporation's ability to compel the conversion of the Series G Preferred Stock is the issuance of a minimum amount of additional capital, subject to terms, other than the price per share, reasonably acceptable to the U.S. Treasury in its sole discretion. On September 16, 2010, the Corporation filed a registration statement for a

proposed underwritten offering of \$500 million of its common stock with the SEC. Thereafter, it amended the registration statement to lower the size of the offering to \$350 million as a result of the negotiation of an amendment to the exchange agreement with the U.S Treasury.

During the fourth quarter of 2010, the U.S. Treasury agreed to a reduction from \$500 million to \$350 million in the size of the capital raise required to satisfy the remaining substantive condition to compel the conversion of the Series G Preferred Stock owned by the U.S. Treasury into shares of common stock. Additionally, the U.S. Treasury agreed to extend to October 7, 2011, the date by when the Corporation is required to complete an equity raise in order to compel conversion of the Series G Preferred Stock into shares of common stock. In connection with the negotiation of this reduction, the Corporation agreed to a reduction in the previously agreed upon discount of the liquidation preference of the Series G Preferred Stock from 35% to 25%, thus, increasing the number of shares of common stock into which the Series G Preferred Stock. Based on an initial conversion rate of 68.9465 shares of common stock for each share of Series G Preferred Stock(calculated by dividing \$750, or a discount of 25% from the \$1,000 liquidation preference per share of Series G Preferred Stock, by the initial conversion price of \$10.878 per share, which is subject to adjustment), the number of shares into which the Series G Preferred Stock would be convertible would increase from 25.3 million to 29.2 million shares of common stock. As a result of the change in the discount, a non-cash adjustment of \$11.3 million was recorded in the fourth quarter of 2010 as an acceleration of the Series G Preferred Stock discount accretion.

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The value of the base preferred stock component of the Series G Preferred Stock was determined using a discounted cash flow method and applying a discount rate. The cash flows, which consist of the sum of the discounted quarterly dividends plus the principal repayment, were discounted considering the Corporation's credit rating. The short and long call options were valued using a Cox-Rubinstein binomial option pricing model-based methodology. The valuation methodology considered the likelihood of option conversions under different scenarios, and the valuation interactions of the various components under each scenario. The difference from the par amount of the Series G Preferred Stock is accreted to preferred stock over 7 years using the interest method with a corresponding adjustment to preferred dividends.

The Series G Preferred Stock qualifies as Tier 1 regulatory capital. Cumulative dividends on the Series G Preferred Stock accrue on the liquidation preference on a quarterly basis at a rate of 5% per annum for the first five years, and thereafter at a rate of 9% per annum, but will only be paid when, as and if declared by the Corporation's Board of Directors out of assets legally available therefore. The Series G Preferred Stock ranks *pari passu* with the Corporation's existing Series A through E preferred stock in terms of dividend payments and distributions upon liquidation, dissolution and winding up of the Corporation. The exchange agreement relating to the issuance of the Series G Preferred Stock limits the payment of dividends on common stock, including limiting regular quarterly cash dividends to an amount not exceeding the last quarterly cash dividend paid per share, or the amount publicly announced (if lower), on common stock prior to October 14, 2008, which is \$1.05 per share.

Additionally, the Corporation issued an amended 10-year warrant (the Warrant) to the U.S. Treasury to purchase 389,483 shares of the Corporation's common stock at an initial exercise price of \$10.878 per share instead of the exercise price on the original warrant of \$154.05 per share. The Warrant has a 10-year term and is exercisable at any time. The exercise price and the number of shares issuable upon exercise of the Warrant are subject to certain anti-dilution adjustments.

The possible future issuance of equity securities through the exercise of the Warrant could affect the Corporation's current stockholders in a number of ways, including by:

- diluting the voting power of the current holders of common stock (the shares underlying the warrant represent approximately 2% of the Corporation's shares of common stock as of March 31, 2011);

- diluting the earnings per share and book value per share of the outstanding shares of common stock; and

- making the payment of dividends on common stock more expensive.

As mentioned above the Corporation stopped paying dividends for common and all its outstanding series of preferred stock. This suspension was effective with the dividends for the month of August 2009 on the Corporation's five outstanding series of non-cumulative preferred stock and dividends on the Corporation's then outstanding Series F Preferred Stock and the Corporation's common stock. Prior to any resumption of the payment of dividends on or repurchases of any of the remaining outstanding noncumulative preferred stock or common stock, the Corporation must comply with the terms of the Series G Preferred Stock. In addition, prior to the repurchase of any stock for cash, the Corporation must obtain the consent of the U.S. Treasury under certain circumstances.

Stock repurchase plan and treasury stock

The Corporation has a stock repurchase program under which, from time to time, it repurchases shares of common stock in the open market and holds them as treasury stock. No shares of common stock were repurchased during the first quarter of 2011 and 2010 by the Corporation. As of March 31, 2011 and December 31, 2010, of the total amount of common stock repurchased in prior years, 659,853 shares were held as treasury stock and were available for general corporate purposes.

Legal surplus

The Banking Act of the Commonwealth of Puerto Rico requires that a minimum of 10% of FirstBank's net income for the year be transferred to legal surplus until such surplus equals the total of paid-in-capital on common and preferred stock. Amounts transferred to the legal surplus account from the retained earnings account are not available for distribution to the stockholders.

18 REGULATORY MATTERS

The Corporation is subject to various regulatory capital requirements imposed by the federal banking agencies. Failure to meet minimum capital requirements can result in certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Corporation's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Corporation must meet specific capital guidelines that involve quantitative measures of the Corporation's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting

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practices. The Corporation's capital amounts and classification are also subject to qualitative judgment by the regulators about components, risk weightings and other factors.

Capital standards established by regulations require the Corporation to maintain minimum amounts and ratios for Leverage (Tier 1 capital to average total assets) and ratios of Tier 1 Capital to Risk-Weighted Assets and Total Capital to Risk-Weighted Assets as defined in the regulations. The total amount of risk-weighted assets is computed by applying risk-weighting factors to the Corporation's assets and certain off-balance sheet items, which generally vary from 0% to 100% depending on the nature of the asset.

Effective June 2, 2010, FirstBank, by and through its Board of Directors, entered into the FDIC Order with the FDIC and the Office of the Commissioner of Financial Institutions of Puerto Rico. This Order provides for various things, including (among other things) the following: (1) having and retaining qualified management; (2) increased participation in the affairs of FirstBank by its board of directors; (3) development and implementation by FirstBank of a capital plan to attain a leverage ratio of at least 8%, a Tier 1 risk-based capital ratio of at least 10% and a total risk-based capital ratio of at least 12%; (4) adoption and implementation of strategic, liquidity and fund management and profit and budget plans and related projects within certain timetables set forth in the Order and on an ongoing basis; (5) adoption and implementation of plans for reducing FirstBank's positions in certain classified assets and delinquent and non-accrual loans within timeframes set forth in the Order; (6) refraining from lending to delinquent or classified borrowers already obligated to FirstBank on any extensions of credit so long as such credit remains uncollected, except where FirstBank's failure to extend further credit to a particular borrower would be detrimental to the best interests of FirstBank, and any such additional credit is approved by the FirstBank's board of directors; (7) refraining from accepting, increasing, renewing or rolling over brokered deposits without the prior written approval of the FDIC; (8) establishment of a comprehensive policy and methodology for determining the allowance for loan and lease losses and the review and revision of FirstBank's loan policies, including the non-accrual policy; and (9) adoption and implementation of adequate and effective programs of independent loan review, appraisal compliance and an effective policy for managing FirstBank's sensitivity to interest rate risk. The foregoing summary is not complete and is qualified in all respects by reference to the actual language of the FDIC Order. Although all the regulatory capital ratios exceeded the established "well capitalized" levels at March 31, 2011, because of the FDIC Order with the FDIC, FirstBank cannot be treated as "well capitalized" institution under regulatory guidance.

Effective June 3, 2010, First BanCorp entered into the Written Agreement with the FED. The Agreement provides, among other things, that the holding company must serve as a source of strength to FirstBank, and that, except upon consent of the FED, (1) the holding company may not pay dividends to stockholders or receive dividends from FirstBank, (2) the holding company and its nonbank subsidiaries may not make payments on trust preferred securities or subordinated debt, and (3) the holding company cannot incur, increase or guarantee debt or repurchase any capital securities. The Written Agreement also requires that the holding company submit a capital plan which reflects sufficient capital at First BanCorp on a consolidated basis, which must be acceptable to the FED, and follow certain guidelines with respect to the appointment or change in responsibilities of senior officers. The foregoing summary is not complete and is qualified in all respects by reference to the actual language of the Written Agreement.

The Corporation submitted its capital plan setting forth how it plans to improve capital positions to comply with the FDIC Order and the Written Agreement over time. Additional information about, the Corporation's achievement of various aspects of the Capital Plan and the terms of the Capital Plan are described above in Note 1.

In addition to the Capital Plan, the Corporation has submitted to its regulators a liquidity and brokered deposit plan, including a contingency funding plan, a non-performing asset reduction plan, a budget and profit plan, a strategic plan and a plan for the reduction of classified and special mention assets. Further, the Corporation has reviewed and enhanced the Corporation's loan review program, various credit policies, the Corporation's treasury and investments policy, the Corporation's asset classification and allowance for loan and lease losses and non-accrual policies, the Corporation's charge-off policy and the Corporation's appraisal program. The Agreements also require the submission to the regulators of quarterly progress reports.

The FDIC Order imposes no other restrictions on the FirstBank's products or services offered to customers, nor does it or the Written Agreement impose any type of penalties or fines upon FirstBank or the Corporation. Concurrent with the FDIC Order, the FDIC has granted FirstBank temporary waivers to enable it to continue accessing the

brokered deposit market through June 30, 2011. FirstBank will request approvals for future periods.

19 INCOME TAXES

Income tax expense includes Puerto Rico and Virgin Islands income taxes as well as applicable U.S. federal and state taxes. The Corporation is subject to Puerto Rico income tax on its income from all sources. As a Puerto Rico corporation, First BanCorp is treated as a foreign corporation for U.S. income tax purposes and is generally subject to United States income tax only on its income from sources within the United States or income effectively connected with the conduct of a trade or business within the United States. Any such tax paid is creditable, within certain conditions and limitations, against the Corporation's Puerto Rico tax liability. The Corporation is also subject to U.S. Virgin Islands taxes on its income from sources within that jurisdiction. Any such tax paid is also creditable against the Corporation's Puerto Rico tax liability, subject to certain conditions and limitations.

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Under the Puerto Rico Internal Revenue Code of 1994, as amended (the PR Code), the Corporation and its subsidiaries are treated as separate taxable entities and are not entitled to file consolidated tax returns and, thus, the Corporation is not able to utilize losses from one subsidiary to offset gains in another subsidiary. Accordingly, in order to obtain a tax benefit from a net operating loss, a particular subsidiary must be able to demonstrate sufficient taxable income within the applicable carry forward period (7 years under the PR Code). The PR Code provides a dividend received deduction of 100% on dividends received from controlled subsidiaries subject to taxation in Puerto Rico and 85% on dividends received from other taxable domestic corporations. Dividend payments from a U.S. subsidiary to the Corporation are subject to a 10% withholding tax based on the provisions of the U.S. Internal Revenue Code.

Under the PR Code, First BanCorp is subject to a maximum statutory tax rate of 39%. In 2009 the Puerto Rico Government approved Act No. 7 (the Act), to stimulate Puerto Rico's economy and to reduce the Puerto Rico Government's fiscal deficit. The Act imposes a series of temporary and permanent measures, including the imposition of a 5% surtax over the total income tax determined, which is applicable to corporations, among others, whose combined income exceeds \$100,000, effectively resulting in an increase in the maximum statutory tax rate from 39% to 40.95% and an increase in the capital gain statutory tax rate from 15% to 15.75%. These temporary measures are effective for tax years that commenced after December 31, 2008 and before January 1, 2012. The PR Code also includes an alternative minimum tax of 22% that applies if the Corporation's regular income tax liability is less than the alternative minimum tax requirements.

The Corporation has maintained an effective tax rate lower than the maximum statutory rate mainly by investing in government obligations and mortgage-backed securities exempt from U.S. and Puerto Rico income taxes and by doing business through International Banking Entity (IBE) of the Bank (FirstBank IBE) and through the Bank's subsidiary, FirstBank Overseas Corporation, in which the interest income and gain on sales is exempt from Puerto Rico and U.S. income taxation. Under the Act, all IBE are subject to the special 5% tax on their net income not otherwise subject to tax pursuant to the PR Code. This temporary measure is also effective for tax years that commenced after December 31, 2008 and before January 1, 2012. FirstBank IBE and FirstBank Overseas Corporation were created under the International Banking Entity Act of Puerto Rico, which provides for total Puerto Rico tax exemption on net income derived by IBEs operating in Puerto Rico. IBEs that operate as a unit of a bank pay income taxes at normal rates to the extent that the IBEs' net income exceeds 20% of the bank's total net taxable income.

On January 31, 2011, the Puerto Rico Government approved Act No. 1, which repealed the 1994 PR Code and replaces it with the Puerto Rico Internal Revenue Code of 2010 (the 2010 PR Code). The provisions of the 2010 Code are generally applicable to taxable years commencing after December 31, 2010. The matters discussed above are equally applicable under the 2010 Code except that the maximum corporate tax rate has been reduced from 39% (40.95% for calendar years 2009 and 2010) to 30% (25% for taxable years commencing after December 31, 2013 if certain economic conditions are met by the Puerto Rico economy). Corporations are entitled to elect continue to determine its Puerto Rico income tax responsibility for such 5 year period under the provisions of the 1994 Code.

For the quarter ended March 31, 2011, the Corporation recorded an income tax expense of \$3.6 million compared to an income tax expense of \$6.9 million for the same period in 2010. As a result of the reduction in the statutory income tax rates from 39% to 30% under the new 2010 Code, the Corporation recorded a \$102.0 million reduction in its deferred tax assets and a \$100.0 million reduction in the valuation allowance. Since the majority of the deferred tax assets were reserved prior to 2011, the net charge to the income statement during the first quarter of 2011 attributed to changes in tax rates was approximately \$2.0 million in connection with profitable subsidiaries. As of March 31, 2011, the deferred tax asset, net of a valuation allowance of \$355.4 million, amounted to \$7.7 million compared to \$9.3 million as of December 31, 2010. The Corporation continued to reserve deferred tax assets created in connection with the operations of its banking subsidiary, FirstBank.

Accounting for income taxes requires that companies assess whether a valuation allowance should be recorded against their deferred tax asset based on the consideration of all available evidence, using a more likely than not realization standard. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount that is more likely than not to be realized. In making such assessment, significant weight is to be given to evidence that can be objectively verified, including both positive and negative evidence. The accounting for income taxes

guidance requires the consideration of all sources of taxable income available to realize the deferred tax asset, including the future reversal of existing temporary differences, future taxable income exclusive of the reversal of temporary differences and carryforwards, taxable income in carryback years and tax planning strategies. In estimating taxes, management assesses the relative merits and risks of the appropriate tax treatment of transactions taking into account statutory, judicial and regulatory guidance, and recognizes tax benefits only when deemed probable of realization.

In assessing the weight of positive and negative evidence, a significant negative factor that resulted in increases of the valuation allowance was that the Corporation's banking subsidiary, FirstBank Puerto Rico, continues in a three-year historical cumulative loss position as of the end of the first quarter of 2011, and has projected to be in a loss position for the remaining of 2011. As of March 31, 2011, management concluded that \$7.7 million of the deferred tax asset will be realized. The Corporation's deferred tax assets for which it has not established a valuation allowance relate to profitable subsidiaries and to amounts that can be realized through future reversals of existing taxable temporary differences. To the extent the realization of a portion, or all, of the tax asset becomes more

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likely than not based on changes in circumstances (such as, improved earnings, changes in tax laws or other relevant changes), a reversal of that portion of the deferred tax asset valuation allowance will then be recorded.

The tax effect of the unrealized holding gain or loss on securities available-for-sale, excluding that on securities held by the Corporation's international banking entities which is exempt, was computed based on a 15% capital gain tax rate, and is included in accumulated other comprehensive income as part of stockholders' equity.

The FASB guidance prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of income tax uncertainties with respect to positions taken or expected to be taken on income tax returns. Under the authoritative accounting guidance, income tax benefits are recognized and measured based upon a two-step model: 1) a tax position must be more likely than not to be sustained based solely on its technical merits in order to be recognized, and 2) the benefit is measured as the largest dollar amount of that position that is more likely than not to be sustained upon settlement. The difference between the benefit recognized in accordance with this model and the tax benefit claimed on a tax return is referred to as an UTB.

The Corporation classified all interest and penalties, if any, related to tax uncertainties as income tax expense. The amount of UTBs may increase or decrease for various reasons, including changes in the amounts for current tax year positions, the expiration of open income tax returns due to the expiration of statutes of limitations, changes in management's judgment about the level of uncertainty, the status of examinations, litigation and legislative activity and the addition or elimination of uncertain tax positions. There were no UTBs outstanding as of March 31, 2011 and December 31, 2010.

20 FAIR VALUE***Fair Value Option***

FASB authoritative guidance permits the measurement of selected eligible financial instruments at fair value.

Medium-Term Notes

The Corporation elected the fair value option for certain medium term notes that were hedged with interest rate swaps that were previously designated for fair value hedge accounting. As of March 31, 2011 and December 31, 2010, these medium-term notes with a principal balance of \$15.4 million, had a fair value of \$12.4 million and \$11.8 million, respectively, recorded in notes payable. Interest paid/accrued on these instruments is recorded as part of interest expense and the accrued interest is part of the fair value of the notes. Electing the fair value option allows the Corporation to eliminate the burden of complying with the requirements for hedge accounting (e.g., documentation and effectiveness assessment) without introducing earnings volatility.

Medium-term notes for which the Corporation elected the fair value option were priced using observable market data in the institutional markets.

Fair Value Measurement

The FASB authoritative guidance for fair value measurement defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This guidance 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. Three levels of inputs may be used to measure fair value:

- Level 1** Valuations of Level 1 assets and liabilities are obtained from readily available pricing sources for market transactions involving identical assets or liabilities. Level 1 assets and liabilities include equity securities that are traded in an active exchange market, as well as certain U.S. Treasury and other U.S. government and agency securities and corporate debt securities that are traded by dealers or brokers in active markets.
- Level 2** Valuations of Level 2 assets and liabilities are based on observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include (i) mortgage-backed securities for which the fair value is estimated based on the value of identical or comparable assets, (ii) debt securities with quoted prices that are traded less frequently than exchange-traded instruments and (iii) derivative contracts and financial liabilities (e.g., medium-term

notes elected to be measured at fair value) whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

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Level 3 Valuations of Level 3 assets and liabilities are based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models for which the determination of fair value requires significant management judgment or estimation.

For 2011, there have been no transfers into or out of Level 1 and Level 2 measurement of the fair value hierarchy.

Estimated 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 Corporation.

The estimated fair value is subjective in nature and involves uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in the underlying assumptions used in calculating fair value could significantly affect the results. In addition, the fair value estimates are based on outstanding balances without attempting to estimate the value of anticipated future business.

The following table presents the estimated fair value and carrying value of financial instruments as of March 31, 2011 and December 31, 2010.

	Financial Condition 3/31/2011	Fair Value Estimated 3/31/2011	Financial Condition 12/31/2010	Fair Value Estimated 12/31/2010
	(In thousands)			
Assets:				
Cash and due from banks and money market investments	\$ 873,294	\$ 873,294	\$ 370,283	\$ 370,283
Investment securities available for sale	2,724,167	2,724,167	2,744,453	2,744,453
Investment securities held to maturity			453,387	476,516
Other equity securities	99,060	99,060	55,932	55,932
Loans held for sale	305,494	312,253	300,766	300,766
Loans, held for investment	11,089,775		11,655,436	
Less: allowance for loan and lease losses	(561,695)		(553,025)	
Loans held for investment, net of allowance	10,528,080	10,019,395	11,102,411	10,581,221
Derivatives, included in assets	2,556	2,556	1,905	1,905
Liabilities:				
Deposits	11,716,436	11,837,155	12,059,110	12,207,613
Securities sold under agreements to repurchase	1,400,000	1,507,010	1,400,000	1,513,338
Advances from FHLB	540,440	560,436	653,440	677,866
Notes Payable	27,837	25,702	26,449	24,909
Other borrowings	231,959	122,722	231,959	71,488
Derivatives, included in liabilities	7,276	7,276	6,701	6,701

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Assets and liabilities measured at fair value on a recurring basis, including financial liabilities for which the Corporation has elected the fair value option, are summarized below:

(In thousands)	As of March 31, 2011				As of December 31, 2010			
	Fair Value Measurements Using			Assets / Liabilities at Fair Value	Fair Value Measurements Using			Assets / Liabilities at Fair Value
Level 1	Level 2	Level 3	Level 1		Level 2	Level 3		
Assets:								
Securities available for sale :								
Equity securities	\$ 47	\$	\$	\$ 47	\$ 59	\$	\$	\$ 59
U.S. Treasury Securities	615,793			615,793	608,714			608,714
Non-callable U.S. agency debt	303,704			303,704	304,257			304,257
Callable U.S. agency debt and MBS		1,573,119		1,573,119		1,622,265		1,622,265
Puerto Rico Government Obligations		158,771	3,083	161,854		134,165	2,676	136,841
Private label MBS			68,355	68,355			72,317	72,317
Corporate bonds			1,295	1,295				
Derivatives, included in assets:								
Interest rate swap agreements		316		316		351		351
Purchased interest rate cap agreements		1		1		1		1
Purchased options used to manage exposure to the stock market on embedded stock indexed options		2,207		2,207		1,553		1,553
Forward Contracts		32		32				

Liabilities:				
Medium-term notes	12,437	12,437	11,842	11,842
Derivatives, included in liabilities:				
Interest rate swap agreements	4,813	4,813	5,192	5,192
Written interest rate cap agreements	1	1	1	1
Embedded written options on stock index deposits and notes payable	2,167	2,167	1,508	1,508
Forward Contracts	296	296		

Changes in Fair Value for items Measured at Fair Value Pursuant to Election of the Fair Value Option For the Quarter ended March 31, 2011 2010 Unrealized Gains and Interest Expense included in Current-Period Earnings (1)

(In thousands)

Medium-term notes	\$	(824)	\$	(1,029)
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(1) Changes in fair value for the quarter ended March 31, 2011 and 2010 include interest expense on medium-term notes of \$0.2 million and \$0.1 million, respectively. Interest expense on medium-term notes that have been elected to be carried at fair value are recorded in interest expense in the Consolidated Statement of Loss based on their contractual coupons.

The table below presents a reconciliation for all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the quarters ended March 31, 2011 and 2010.

Level 3 Instruments Only	Total Fair Value Measurements (Quarter Ended March 31, 2011) Securities	Total Fair Value Measurements (Quarter Ended March 31, 2010) Securities Available For Sale⁽¹⁾
<i>(In thousands)</i>	Available For Sale⁽¹⁾	Derivatives⁽²⁾
Beginning balance	\$ 74,993	\$ 4,199
Total gains or (losses) (realized/unrealized):		
Included in earnings		(712)
Included in other comprehensive income	46	323
Held-to-Maturity investment securities reclassified to Available-for-Sale	2,000	

Principal repayments and amortization		(4,306)			(3,794)
Ending balance	\$	72,733	\$	3,487	\$ 80,883

- (1) Amounts mostly related to private label mortgage-backed securities.
- (2) Amounts related to the valuation of interest rate cap agreements. The counterparty to these interest rate cap agreements failed on April 30, 2010 and was acquired by another financial institution in an FDIC assisted transaction. The Corporation currently has a claim with the FDIC.
- The table below summarizes changes in unrealized gains and losses recorded in earnings for the quarter ended March 31, 2010 for Level 3 assets and liabilities that are still held at the end of the period.

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Level 3 Instruments Only <i>(In thousands)</i>	Changes in Unrealized Losses (Quarter Ended March 31, 2010) Derivatives	
Changes in unrealized losses relating to assets still held at reporting date^{(1) (2)}:		
Interest income on loans	\$	(15)
Interest income on investment securities		(697)
	\$	(712)

(1) Amounts represent valuation of interest rate cap agreements

(2) Unrealized losses of \$0.3 million on Level 3 available-for-sale securities was recognized as part of other comprehensive income for the quarter ended March 31, 2010.

Additionally, fair value is used on a non-recurring basis to evaluate certain assets in accordance with GAAP. Adjustments to fair value usually result from the application of lower-of-cost-or-market accounting (e.g., loans held for sale carried at the lower of cost or fair value and repossessed assets) or write-downs of individual assets (e.g., goodwill, loans).

As of March 31, 2011, impairment or valuation adjustments were recorded for assets recognized at fair value on a non-recurring basis as shown in the following table:

	Carrying value as of March 31, 2011			Losses recorded for the Quarter Ended
	Level 1	Level 2	Level 3	March 31, 2011
			(In thousands)	
Loans receivable (1)	\$	\$	\$1,331,634	\$ 95,786
Other Real Estate Owned (2)			91,948	2,975

(1) Mainly impaired commercial and construction loans. The impairment was generally measured based on the fair value of the collateral. The fair values are derived from appraisals that take into consideration prices in observed transactions involving similar assets in similar locations but adjusted for specific characteristics and assumptions of the collateral (e.g. absorption rates), which are not market observable.

(2) The fair value is derived from appraisals that take into consideration prices in observed transactions involving similar assets in similar locations but adjusted for specific characteristics and assumptions of the properties (e.g. absorption rates), which are not market observable. Losses are related to market valuation adjustments after the transfer from the loan to the OREO portfolio.

As of March 31, 2010, impairment or valuation adjustments were recorded for assets recognized at fair value on a non-recurring basis as shown in the following table:

**Losses recorded
for**

	Carrying value as of March 31, 2010			the Quarter
	Level			Ended
	1	Level 2	Level 3	March 31, 2010
	(In thousands)			
Loans receivable (1)	\$	\$	\$1,390,467	\$ 137,767
Other Real Estate Owned (2)			73,444	1,195
Loans held for sale (3)		19,927		140

- (1) Mainly impaired commercial and construction loans. The impairment was generally measured based on the fair value of the collateral.

The fair values are derived from appraisals that take into consideration prices in observed transactions involving similar assets in similar locations but adjusted for specific characteristics and assumptions of the collateral (e.g. absorption rates), which are not market observable.

- (2) The fair value is derived from appraisals that take into consideration prices in observed transactions involving similar assets in similar locations but adjusted for specific characteristics and assumptions of the properties (e.g. absorption rates), which are not market observable. Losses are related to market valuation adjustments after the transfer from the loan to the Other Real Estate Owned (OREO) portfolio.

- (3) Fair value is primarily derived from quotations based on the mortgage-backed securities market.

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The following is a description of the valuation methodologies used for instruments for which an estimated fair value is presented as well as for instruments for which the Corporation has elected the fair value option. The estimated fair value was calculated using certain facts and assumptions, which vary depending on the specific financial instrument.

Cash and due from banks and money market investments

The carrying amounts of cash and due from banks and money market investments are reasonable estimates of their fair value. Money market investments might include held-to-maturity U.S. Government obligations, which have a contractual maturity of three months or less. The fair value of these securities is based on quoted market prices in active markets that incorporate the risk of nonperformance.

Investment securities available for sale and held to maturity

The fair value of investment securities is the market value based on quoted market prices (as is the case with equity securities, U.S. Treasury notes and non-callable U.S. Agency debt securities), when available, or market prices for identical or comparable assets (as is the case with MBS and callable U.S. agency debt) that are based on observable market parameters including benchmark yields, reported trades, quotes from brokers or dealers, issuer spreads, bids, offers and reference data including market research operations. Observable prices in the market already consider the risk of nonperformance. If listed prices or quotes are not available, fair value is based upon models that use unobservable inputs due to the limited market activity of the instrument, as is the case with certain private label mortgage-backed securities held by the Corporation.

Private label MBS are collateralized by fixed-rate mortgages on single-family residential properties in the United States; the interest rate on the securities is variable, tied to 3-month LIBOR and limited to the weighted-average coupon of the underlying collateral. The market valuation represents the estimated net cash flows over the projected life of the pool of underlying assets applying a discount rate that reflects market observed floating spreads over LIBOR, with a widening spread bias on a nonrated security. The market valuation is derived from a model that utilizes relevant assumptions such as prepayment rate, default rate, and loss severity on a loan level basis. The Corporation modeled the cash flow from the fixed-rate mortgage collateral using a static cash flow analysis according to collateral attributes of the underlying mortgage pool (i.e. loan term, current balance, note rate, rate adjustment type, rate adjustment frequency, rate caps, others) in combination with prepayment forecasts obtained from a commercially available prepayment model (ADCO). The variable cash flow of the security is modeled using the 3-month LIBOR forward curve. Loss assumptions were driven by the combination of default and loss severity estimates, taking into account loan credit characteristics (loan-to-value, state, origination date, property type, occupancy loan purpose, documentation type, debt-to-income ratio, other) to provide an estimate of default and loss severity. Refer to Note 4 for additional information about assumptions used in the valuation of private label MBS.

Other equity securities

Equity or other securities that do not have a readily available fair value are stated at the net realizable value, which management believes is a reasonable proxy for their fair value. This category is principally composed of stock that is owned by the Corporation to comply with FHLB regulatory requirements. Their realizable value equals their cost as these shares can be freely redeemed at par. Also includes, the Corporation's 35% interest in a joint venture. The initial value of \$47.6 million represents 35% of all the assets of the joint venture. Please refer to Note 11 for additional information.

Loans receivable, including loans held for sale

The fair value of loans held for investment and for mortgage loans held for sale was estimated using discounted cash flow analyses, based on interest rates currently being offered for loans with similar terms and credit quality and with adjustments that the Corporation's management believes a market participant would consider in determining fair value. Loans were classified by type such as commercial, residential mortgage, and automobile. These asset categories were further segmented into fixed- and adjustable-rate categories. The fair values of performing fixed-rate and adjustable-rate loans were calculated by discounting expected cash flows through the estimated maturity date. Loans with no stated maturity, like credit lines, were valued at book value. Prepayment assumptions were considered for non-residential loans. For residential mortgage loans, prepayment estimates were based on recent historical prepayment experience of the Corporation's residential mortgage portfolio. Discount rates were based on the Treasury

and LIBOR/Swap Yield Curves at the date of the analysis, and included appropriate adjustments for expected credit losses and liquidity. For impaired collateral dependent loans, the impairment was primarily measured based on the fair value of the collateral, which is derived from appraisals that take into consideration prices in observable transactions involving similar assets in similar locations. For construction, commercial mortgage and commercial loans transferred to held for sale during the fourth quarter of 2010, the fair value equals the established sales price of these loans. The Corporation completed the sale of substantially all of these loans on February 16, 2011.

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The estimated fair value of demand deposits and savings accounts, which are deposits with no defined maturities, equals the amount payable on demand at the reporting date. The fair values of retail fixed-rate time deposits, with stated maturities, are based on the present value of the future cash flows expected to be paid on the deposits. The cash flows were based on contractual maturities; no early repayments are assumed. Discount rates were based on the LIBOR yield curve.

The estimated fair value of total deposits excludes the fair value of core deposit intangibles, which represent the value of the customer relationship measured by the value of demand deposits and savings deposits that bear a low or zero rate of interest and do not fluctuate in response to changes in interest rates.

The fair value of brokered CDs, which are included within deposits, is determined using discounted cash flow analyses over the full term of the CDs. The valuation uses a Hull-White Interest Rate Tree approach, an industry-standard approach for valuing instruments with interest rate call options. The fair value of the CDs is computed using the outstanding principal amount. The discount rates used are based on US dollar LIBOR and swap rates. At-the-money implied swaption volatility term structure (volatility by time to maturity) is used to calibrate the model to current market prices. The fair value does not incorporate the risk of nonperformance, since interests in brokered CDs are generally sold by brokers in amounts of less than \$100,000 and, therefore, insured by the FDIC.

Securities sold under agreements to repurchase

Some repurchase agreements reprice at least quarterly, and their outstanding balances are estimated to be their fair value. Where longer commitments are involved, fair value is estimated using exit price indications of the cost of unwinding the transactions as of the end of the reporting period. Securities sold under agreements to repurchase are fully collateralized by investment securities.

Advances from FHLB

The fair value of advances from FHLB with fixed maturities is determined using discounted cash flow analyses over the full term of the borrowings, using indications of the fair value of similar transactions. The cash flows assume no early repayment of the borrowings. Discount rates are based on the LIBOR yield curve. For advances from FHLB that reprice quarterly, their outstanding balances are estimated to be their fair value. Advances from FHLB are fully collateralized by mortgage loans and, to a lesser extent, investment securities.

Derivative instruments

The fair value of most of the derivative instruments is based on observable market parameters and takes into consideration the credit risk component of paying counterparties when appropriate, except when collateral is pledged. That is, on interest rate swaps, the credit risk of both counterparties is included in the valuation; and, on options and caps, only the seller's credit risk is considered. The Hull-White Interest Rate Tree approach is used to value the option components of derivative instruments, and discounting of the cash flows is performed using US dollar LIBOR-based discount rates or yield curves that account for the industry sector and the credit rating of the counterparty and/or the Corporation. Derivatives include interest rate swaps used for protection against rising interest rates. For these interest rate swaps, a credit component was not considered in the valuation since the Corporation has fully collateralized with investment securities any mark to market loss with the counterparty and, if there were market gains, the counterparty had to deliver collateral to the Corporation.

Although most of the derivative instruments are fully collateralized, a credit spread is considered for those that are not secured in full. The cumulative mark-to-market effect of credit risk in the valuation of derivative instruments resulted in an unrealized gain of approximately \$0.6 million as of March 31, 2011, which includes an unrealized loss of \$0.2 million recorded in the first quarter of 2011 and an unrealized loss of \$0.1 million for the first quarter of 2010.

Term notes payable

The fair value of term notes is determined using a discounted cash flow analysis over the full term of the borrowings. This valuation also uses the Hull-White Interest Rate Tree approach to value the option components of the term notes. The model assumes that the embedded options are exercised economically. The fair value of medium-term notes is computed using the notional amount outstanding. The discount rates used in the valuations are based on US dollar LIBOR and swap rates. At-the-money implied swaption volatility term structure (volatility by time to maturity) is used to calibrate the model to current market prices and value the cancellation option in the term notes.

For the medium-term notes, the credit risk is measured using the difference in yield curves between swap rates and a yield curve that considers the industry and credit rating of the Corporation as issuer of the note at a tenor comparable to the time to maturity of the note and option. The net loss from fair value changes attributable to the Corporation's own credit to the medium-term notes for which the Corporation has elected the fair value option recorded for the first quarter of 2011 amounted to \$0.6 million, compared to an unrealized loss of \$1.0 million for the first quarter of 2010. The cumulative mark-to-market unrealized gain on the medium-term notes since measured at fair value attributable to credit risk amounted to \$3.1 million as of March 31, 2011.

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Other borrowings consist of junior subordinated debentures. Projected cash flows from the debentures were discounted using the LIBOR yield curve plus a credit spread. This credit spread was estimated using the difference in yield curves between Swap rates and a yield curve that considers the industry and credit rating of the Corporation as issuer of the note at a tenor comparable to the time to maturity of the debentures.

21 SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash flow information follows:

	Quarter Ended March 31,	
	2011	2010
	(In thousands)	
Cash paid for:		
Interest on borrowings	\$ 68,257	\$98,088
Income tax	242	
Non-cash investing and financing activities:		
Additions to other real estate owned	28,483	18,930
Additions to auto repossessions	16,691	18,909
Capitalization of servicing assets	1,231	1,686
Loan securitizations	41,474	57,204
Loans sold to a joint venture in exchange for an acquisition loan and an equity interest in the joint venture	183,709	
Reclassification of Held-to-Maturity investment securities to Available-for-Sale	88,751	

22 SEGMENT INFORMATION

Based upon the Corporation's organizational structure and the information provided to the Chief Executive Officer of the Corporation and, to a lesser extent, the Board of Directors, the operating segments are driven primarily by the Corporation's lines of business for its operations in Puerto Rico, the Corporation's principal market, and by geographic areas for its operations outside of Puerto Rico. As of March 31, 2011, the Corporation had six reportable segments: Commercial and Corporate Banking; Mortgage Banking; Consumer (Retail) Banking; Treasury and Investments; United States operations and Virgin Islands operations. Management determined the reportable segments based on the internal reporting used to evaluate performance and to assess where to allocate resources. Other factors such as the Corporation's organizational chart, nature of the products, distribution channels and the economic characteristics of the products were also considered in the determination of the reportable segments.

The Commercial and Corporate Banking segment consists of the Corporation's lending and other services for large customers represented by specialized and middle-market clients and the public sector. The Commercial and Corporate Banking segment offers commercial loans, including commercial real estate and construction loans, and floor plan financings as well as other products such as cash management and business management services. The Mortgage Banking segment's operations consist of the origination, sale and servicing of a variety of residential mortgage loans. The Mortgage Banking segment also acquires and sells mortgages in the secondary markets. In addition, the Mortgage Banking segment includes mortgage loans purchased from other local banks and mortgage bankers. The Consumer (Retail) Banking segment consists of the Corporation's consumer lending and deposit-taking activities conducted mainly through its branch network and loan centers. The Treasury and Investments segment is responsible for the Corporation's investment portfolio and treasury functions executed to manage and enhance liquidity. This segment lends funds to the Commercial and Corporate Banking, Mortgage Banking and Consumer (Retail) Banking segments to finance their lending activities and borrows from those segments and from the United States Operations segment. The Consumer (Retail) Banking and the United States Operations segments also lend funds to other segments. The interest rates charged or credited by Treasury and Investments, the Consumer (Retail) Banking and the United States

Operations segments are allocated based on market rates. The difference between the allocated interest income or expense and the Corporation's actual net interest income from centralized management of funding costs is reported in the Treasury and Investments segment. The United States operations segment consists of all banking activities conducted by FirstBank in the United States mainland, including commercial and retail banking services. The Virgin Islands

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operations segment consists of all banking activities conducted by the Corporation in the U.S. and British Virgin Islands, including commercial and retail banking services and insurance activities.

The accounting policies of the segments are the same as those referred to in Note 1 to the Corporation's financial statements for the year ended December 31, 2010 contained in the Corporation's Annual Report or Form 10-K.

The Corporation evaluates the performance of the segments based on net interest income, the estimated provision for loan and lease losses, non-interest income and direct non-interest expenses. The segments are also evaluated based on the average volume of their interest-earning assets less the allowance for loan and lease losses.

The following table presents information about the reportable segments (in thousands):

	Mortgage Banking	Consumer (Retail) Banking	Commercial and Corporate	Treasury and Investments	United States Operations	Virgin Islands Operations	Total
(In thousands) For the quarter ended March 31, 2011:							
Interest income	\$ 34,880	\$ 43,413	\$ 52,390	\$ 22,630	\$ 12,342	\$ 15,248	\$ 180,903
Net (charge) credit for transfer of funds	(18,692)	1,838	(3,230)	15,505	4,579	(1,631)	(74,624)
Interest expense		(11,505)		(50,691)	(10,797)	(1,631)	(74,624)
Net interest income	16,188	33,746	49,160	(12,556)	6,124	13,617	106,279
Provision for loan and lease losses	(675)	(5,192)	(51,124)		(7,900)	(23,841)	(88,732)
Non-interest income	6,787	6,929	2,220	19,143	143	5,263	40,485
Direct non-interest expenses	(7,815)	(22,355)	(9,153)	(1,476)	(8,602)	(10,069)	(59,470)
Segment income (loss)	\$ 14,485	\$ 13,128	\$ (8,897)	\$ 5,111	\$ (10,235)	\$ (15,030)	\$ (1,438)
Average earnings assets	\$ 2,438,536	\$ 1,492,909	\$ 5,387,552	\$ 3,584,468	\$ 904,348	\$ 910,154	\$ 14,717,967
For the quarter ended March 31, 2010:							
Interest income	\$ 40,026	\$ 47,562	\$ 58,842	\$ 42,774	\$ 13,930	\$ 17,854	\$ 220,988
Net (charge) credit	(25,327)	2,140	(6,826)	30,013			

for transfer of funds							
Interest expense		(13,568)		(77,740)	(11,267)	(1,550)	(104,125)
Net interest income	14,699	36,134	52,016	(4,953)	2,663	16,304	116,863
Provision for loan and lease losses	(16,014)	(12,493)	(59,448)		(71,202)	(11,808)	(170,965)
Non-interest income	2,251	7,307	1,602	30,585	154	3,427	45,326
Direct non-interest expenses	(8,095)	(24,000)	(17,586)	(1,612)	(9,317)	(11,009)	(71,619)
Segment (loss) income	\$ (7,159)	\$ 6,948	\$ (23,416)	\$ 24,020	\$ (77,702)	\$ (3,086)	\$ (80,395)

Average earnings assets \$ 2,708,763 \$ 1,667,043 \$ 6,452,243 \$ 5,466,721 \$ 1,261,836 \$ 1,041,767 \$ 18,598,373

The following table presents a reconciliation of the reportable segment financial information to the consolidated totals:

	Quarter ended March 31,	
	2011	2010
	(In thousands)	
Net loss:		
Total loss for segments and other	\$ (1,438)	\$ (80,395)
Other operating expenses	(23,396)	(19,743)
Loss before income taxes	(24,834)	(100,138)
Income tax expense	(3,586)	(6,861)
Total consolidated net loss	\$ (28,420)	\$ (106,999)
Average assets:		
Total average earning assets for segments	\$ 14,717,967	\$ 18,598,373
Average non-earning assets	661,017	716,679
Total consolidated average assets	\$ 15,378,984	\$ 19,315,052

23 COMMITMENTS AND CONTINGENCIES

The Corporation enters into financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments may include commitments to extend credit and commitments to sell mortgage loans at fair value. As of March 31, 2011, commitments to extend credit amounted to approximately \$667.9 million and commercial and financial standby letters of credit amounted to approximately \$80.5 million. Commitments to extend credit are agreements to lend to a

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customer as long as there is no violation of any conditions established in the contract. Commitments generally have fixed expiration dates or other termination clauses. For most of the commercial lines of credit, the Corporation has the option to reevaluate the agreement prior to additional disbursements. In the case of credit cards and personal lines of credit, the Corporation can at any time and without cause, cancel the unused credit facility. Generally, the Corporation's mortgage banking activities do not enter into interest rate lock agreements with prospective borrowers.

Lehman Brothers Special Financing, Inc. (Lehman) was the counterparty to the Corporation on certain interest rate swap agreements. During the third quarter of 2008, Lehman failed to pay the scheduled net cash settlement due to the Corporation, which constituted an event of default under those interest rate swap agreements. The Corporation terminated all interest rate swaps with Lehman and replaced them with other counterparties under similar terms and conditions. In connection with the unpaid net cash settlement due as of March 31, 2011 under the swap agreements, the Corporation has an unsecured counterparty exposure with Lehman, which filed for bankruptcy on October 3, 2008, of approximately \$1.4 million. This exposure was reserved in the third quarter of 2008. The Corporation had pledged collateral of \$63.6 million with Lehman to guarantee its performance under the swap agreements in the event payment there under was required. The book value of pledged securities with Lehman as of December 31, 2010 amounted to approximately \$64.5 million.

The Corporation believes that the securities pledged as collateral should not be part of the Lehman bankruptcy estate given the fact that the posted collateral constituted a performance guarantee under the swap agreements and was not part of a financing agreement, and that ownership of the securities was never transferred to Lehman. Upon termination of the interest rate swap agreements, Lehman's obligation was to return the collateral to the Corporation. During the fourth quarter of 2009, the Corporation discovered that Lehman Brothers, Inc., acting as agent of Lehman, had deposited the securities in a custodial account at JP Morgan Chase, and that, shortly before the filing of the Lehman bankruptcy proceedings, it had provided instructions to have most of the securities transferred to Barclays Capital (Barclays) in New York. After Barclays's refusal to turn over the securities, during December 2009, the Corporation filed a lawsuit against Barclays in federal court in New York demanding the return of the securities.

During February 2010, Barclays filed a motion with the court requesting that the Corporation's claim be dismissed on the grounds that the allegations of the complaint are not sufficient to justify the granting of the remedies therein sought. Shortly thereafter, the Corporation filed its opposition motion. A hearing on the motions was held in court on April 28, 2010. The court, on that date, after hearing the arguments by both sides, concluded that the Corporation's equitable-based causes of action, upon which the return of the investment securities is being demanded, contain allegations that sufficiently plead facts warranting the denial of Barclays' motion to dismiss the Corporation's claim. Accordingly, the judge ordered the case to proceed to trial. Subsequent to the court decision, the district court judge transferred the case to the Lehman bankruptcy court for trial. While the Corporation believes it has valid reasons to support its claim for the return of the securities, the Corporation may not succeed in its litigation against Barclays to recover all or a substantial portion of the securities. Upon such transfer, the Bankruptcy court began to entertain the pre-trial procedures including discovery of evidence. In this regard, an initial scheduling conference was held before the United States Bankruptcy Court for the Southern District of New York on November 17, 2010, at which time a proposed case management plan was approved. Discovery has commenced pursuant to that case management plan and is currently scheduled for completion by September 15, 2011, but this timing is subject to adjustment.

Additionally, the Corporation continues to pursue its claim filed in January 2009 in the proceedings under the Securities Protection Act with regard to Lehman Brothers Incorporated in Bankruptcy Court, Southern District of New York. An estimated loss was not accrued as the Corporation is unable to determine the timing of the claim resolution or whether it will succeed in recovering all or a substantial portion of the collateral or its equivalent value. If additional relevant negative facts become available in future periods, a need to recognize a partial or full reserve of this claim may arise. Considering that the investment securities have not yet been recovered by the Corporation, despite its efforts in this regard, the Corporation has maintained such investments classified as non-performing since the second quarter of 2009.

As of March 31, 2011, First BanCorp and its subsidiaries were defendants in various legal proceedings arising in the ordinary course of business. Management believes that the final disposition of these matters will not have a material adverse effect on the Corporation's financial position, results of operations or cash flows.

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The following condensed financial information presents the financial position of the Holding Company only as of March 31, 2011 and December 31, 2010 and the results of its operations for the quarters ended March 31, 2011 and 2010.

	As of March 31, 2011	As of December 31, 2010
	(In thousands)	
Assets		
Cash and due from banks	\$ 19,760	\$ 42,430
Money market investments		
Investment securities available for sale, at market:		
Equity investments	47	59
Other investment securities	1,300	1,300
Investment in First Bank Puerto Rico, at equity	1,224,020	1,231,603
Investment in First Bank Insurance Agency, at equity	6,659	6,275
Investment in FBP Statutory Trust I	3,093	3,093
Investment in FBP Statutory Trust II	3,866	3,866
Other assets	6,660	5,395
 Total assets	 \$ 1,265,405	 \$ 1,294,021
 Liabilities & Stockholders Equity		
Liabilities:		
Other borrowings	\$ 231,959	\$ 231,959
Accounts payable and other liabilities	6,177	4,103
 Total liabilities	 238,136	 236,062
 Stockholders equity	 1,027,269	 1,057,959
 Total liabilities and stockholders equity	 \$ 1,265,405	 \$ 1,294,021

	Quarter Ended	
	March 31, 2011	March 31, 2010
	(In thousands)	
Income:		
Dividends from FirstBank Puerto Rico	\$	\$ 751
Other income	52	50
	52	801

Expense:

Notes payable and other borrowings	1,718	1,672
Other operating expenses	510	689
	2,228	2,361
Investment-related proceeds and impairments on equity securities	679	(600)
Loss before income taxes and equity in undistributed losses of subsidiaries	(1,497)	(2,160)
Income tax benefit		
Equity in undistributed losses of subsidiaries	(26,923)	(104,839)
Net loss	\$ (28,420)	\$ (106,999)

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25 SUBSEQUENT EVENTS

On April 6, 2011, consistent with the Corporation's deleverage strategy included in the Capital Plan submitted to regulators in the first quarter of 2011, the Corporation sold approximately \$268 million in U.S. Agency MBS for which an approximate \$20 million gain was recognized.

On April 15, 2011, the Corporation sold mortgage loans with an unpaid principal balance of \$282 million to another financial institution. The Corporation recognized a gain of approximately \$6.8 million associated with this transaction in the second quarter of 2011. These loans were reclassified to held for sale in the first quarter of 2011.

The Corporation has performed an evaluation of all other events occurring subsequent to March 31, 2011; management has determined that there are no additional events occurring in this period that required disclosure in or adjustment to the accompanying financial statements.

Table of Contents**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (MD&A)****SELECTED FINANCIAL DATA****(In thousands, except for per share and financial ratios)**

	Quarter Ended March 31,	
	2011	2010
Condensed Income Statement:		
Total interest income	\$ 180,903	\$ 220,988
Total interest expense	74,624	104,125
Net interest income	106,279	116,863
Provision for loan and lease losses	88,732	170,965
Non-interest income	40,485	45,326
Non-interest expenses	82,866	91,362
Loss before income taxes	(24,834)	(100,138)
Income tax expense	(3,586)	(6,861)
Net loss	(28,420)	(106,999)
Net loss attributable to common stockholders	(35,437)	(113,151)

Per Common Share Results (1):

Net loss per share basic	\$ (1.66)	\$ (18.34)
Net loss per share diluted	\$ (1.66)	\$ (18.34)
Cash dividends declared	\$	\$
Average shares outstanding	21,303	6,168
Book value per common share	\$ 28.19	\$ 90.59
Tangible book value per common share (2)	\$ 26.24	\$ 83.45

Selected Financial Ratios (In Percent):**Profitability:**

Return on average assets	(0.75)	(2.25)
Interest rate spread ⁽³⁾	2.63	2.45
Net interest margin ⁽³⁾	2.89	2.73
Return on average total equity	(11.09)	(27.07)
Return on average common equity	(23.42)	(68.06)
Average total equity to average total assets	6.76	8.30
Tangible common equity ratio ⁽²⁾	3.71	2.74
Dividend payout ratio		
Efficiency ratio ⁽⁴⁾	56.46	56.33

Asset Quality:

Allowance for loan and lease losses to period end loans held for investment	5.06	4.33
Net charge-offs (annualized) to average loans	2.74	3.65
Provision for loan and lease losses to net charge-offs	110.83	138.12
Non-performing assets to total assets	9.34 ⁽⁵⁾	9.49

Non-performing loans held for investment to total loans held for investment	11.12	12.35
Allowance to total non-performing loans held for investment	45.55	35.09
Allowance to total non-performing loans held for investment, excluding residential real estate loans	66.78	48.24

Other Information:

Common Stock Price: End of period	\$ 5.00	\$ 36.15
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	As of March 31, 2011	As of December 31, 2010
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Balance Sheet Data:

Total loans	\$11,395,269	\$11,956,202
Allowance for loan and lease losses	561,695	553,025
Money market and investment securities	2,933,880	3,369,332
Intangible assets	41,552	42,141
Deferred tax asset, net	7,669	9,269
Total assets	15,104,090	15,593,077
Deposits	11,716,436	12,059,110
Borrowings	2,200,236	2,311,848
Total preferred equity	426,724	425,009
Total common equity	585,121	615,232
Accumulated other comprehensive loss, net of tax	15,424	17,718
Total equity	1,027,269	1,057,959

- (1) All share and per share data has been adjusted to retroactively reflect the 1-for-15 reverse stock split effected January 7, 2011.
- (2) Non-GAAP measure. Refer to Capital discussion below for additional information of the components and reconciliation of these measures.
- (3) On a tax-equivalent basis and excluding the changes in fair value of derivative instruments and financial liabilities measured at fair value (see Net Interest Income discussion below for a reconciliation of this non-GAAP measure).
- (4) Non-interest expense to the sum of net interest income and non-interest income. The denominator includes non-recurring income and changes in the fair value of derivative instruments and financial instruments measured at fair value.
- (5) Non-performing assets, excluding non-performing loans held for sale, to total assets, excluding non-performing loans transferred to held for sale was 9.30% as of March 31, 2011.

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The following Management's Discussion and Analysis of Financial Condition and Results of Operations relates to the accompanying consolidated unaudited financial statements of First BanCorp (the Corporation or First BanCorp) and should be read in conjunction with such financial statements and the notes thereto.

DESCRIPTION OF BUSINESS**Description of Business**

First BanCorp is a diversified financial holding company headquartered in San Juan, Puerto Rico offering a full range of financial products to consumers and commercial customers through various subsidiaries. First BanCorp is the holding company of FirstBank Puerto Rico (FirstBank or the Bank) and FirstBank Insurance Agency. Through its wholly-owned subsidiaries, the Corporation operates offices in Puerto Rico, the United States and British Virgin Islands and the State of Florida (USA) specializing in commercial banking, residential mortgage loan originations, finance leases, personal loans, small loans, auto loans, insurance agency and broker-dealer activities.

As described in Note 18, Regulatory Matters, FirstBank is currently operating under a Consent Order (the Order) with the Federal Deposit Insurance Corporation (FDIC) and First BanCorp has entered into a Written Agreement (the Written Agreement) and collectively with the Order the Agreements) with the Board of Governors of the Federal Reserve System (the FED or Federal Reserve).

As discussed in Note 1 to the Consolidated Financial Statements, the Corporation has assessed its ability to continue as a going concern and has concluded that, based on current and expected liquidity needs and sources, management expects the Corporation to be able to meet its obligations for a reasonable period of time. If unanticipated market factors emerge, or if the Corporation is unable to raise additional capital or complete identified capital preservation initiatives, successfully execute its strategic operating plans, issue a sufficient amount of brokered deposits or comply with the Order, its banking regulators could take further action, which could include actions that may have a material adverse effect on the Corporation's business, results of operations and financial position, including, the appointment of a conservator or receiver. Also see Liquidity Risk and Capital Adequacy.

OVERVIEW OF RESULTS OF OPERATIONS

First BanCorp's results of operations generally depend primarily upon its net interest income, which is the difference between the interest income earned on its interest-earning assets, including investment securities and loans, and the interest expense incurred on its interest-bearing liabilities, including deposits and borrowings. Net interest income is affected by various factors, including: the interest rate scenario; the volumes, mix and composition of interest-earning assets and interest-bearing liabilities; and the re-pricing characteristics of these assets and liabilities. The Corporation's results of operations also depend on the provision for loan and lease losses, which significantly affected the results for the past two years, non-interest expenses (such as personnel, occupancy, deposit insurance premiums and other costs), non-interest income (mainly service charges and fees on loans and deposits and insurance income), gains (losses) on sales of investments, gains (losses) on mortgage banking activities, and income taxes.

Net loss for the quarter ended March 31, 2011 amounted to \$28.4 million, or \$1.66 loss per diluted common share, compared to a net loss of \$107.0 million, or \$18.34 loss per diluted common share for the quarter ended March 31, 2010. The Corporation's financial results for the first quarter of 2011, as compared to the first quarter of 2010, were principally impacted by (i) a decrease in the provision for loan and lease losses of \$82.2 million primarily related to lower charges to specific reserves, a decrease in the volume non-performing loans as well as reductions in charge-offs and the overall reduction of the loan portfolio, and (ii) a decrease of \$8.5 million in non-interest expenses mainly related to a decrease in the reserve for off-balance sheet exposures such as letters of credit and unfunded commitments as well as a decrease in the FDIC deposit insurance premium. These factors were partially offset by a decrease of \$10.6 million in net interest income primarily related to a decrease in average interest earning assets and a decrease of \$4.8 million in non-interest income mainly related to lower gains on sales of investment securities.

The key drivers of the Corporation's financial results for the quarter ended March 31, 2011 include the following:

Net interest income for the quarter ended March 31, 2011 was \$106.3 million, compared to \$116.9 million for the same period in 2010. The decrease largely due to a decrease in the volume of interest earning assets, consistent with the Corporation's deleveraging initiatives to preserve and improve the Corporation's capital position. Average interest-earning assets decreased by \$3.8 billion when compared to the first quarter of 2010, reflecting a \$1.9 billion reduction in average total loans and leases mainly due to loan sales combined

with non-renewal of maturing government credit facilities and pay-downs; average investment securities and other short-term investments decreased by \$1.9 billion primarily related to sales and prepayments of U.S. agency MBS. Refer to the Net Interest Income discussion below for additional information.

For the first quarter of 2011, the Corporation's provision for loan and lease losses amounted to \$88.7 million, compared to \$171.0 million for the same period in 2010. The decrease in the provision for 2011 was primarily due to lower charges to specific reserves, a decrease in non-performing

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loans, charge-offs and the overall reduction of the loan portfolio. Much of the decrease in the provision is related to the construction and residential mortgage loan portfolios. Refer to the discussions under Provision for loan and lease losses and Risk Management below for an analysis of the allowance for loan and lease losses and non-performing assets and related ratios.

As previously reported, at the end of the 2010 fourth quarter, the Corporation transferred \$447 million of loans (\$335 million of construction loans, \$83 million of commercial mortgage loans and \$29 million of commercial and industrial loans) to held for sale at a value of \$281.6 million. This resulted in charge-offs at the time of transfer of \$165.1 million (\$127.0 million related to construction loans, \$29.5 million related to commercial mortgage loans and \$8.6 million related to commercial and industrial (C&I) loans). The 2010 fourth quarter provision for loan losses included \$102.9 million related to this transfer of loans to loans held for sale. During the first quarter of 2011, these loans with a book value of \$269.3 million were sold at essentially book value. The completion of the loan sale was the main driver of the reduction of \$159.8 million in total non-performing loans during the first quarter of 2011.

For the quarter ended March 31, 2011, the Corporation's non-interest income amounted to \$40.5 million, compared to \$45.3 million for the quarter ended March 31, 2010. The decrease mainly reflects the impact of a \$10.7 million gain on the sale of VISA Class C shares recognized in the first quarter of 2010, partially offset by a \$4.3 million increase in income from mortgage banking activities. The increase in mortgage banking activities is mainly related to a \$5.3 million gain recognized on the bulk sale of \$236 million of performing residential mortgage loans to another financial. Refer to the Non Interest Income discussion below for additional information.

Non-interest expenses for the first quarter of 2011 amounted to \$82.9 million, compared to \$91.4 million for the same period in 2010. The decrease is mainly related to a decrease of \$6.6 million in charges to the reserve for off-balance sheet exposures due to reductions in letters of credit and unfunded loan commitment balances, a decrease of \$3.2 million in the FDIC deposit insurance premium and a \$1.3 million decrease in employee compensation and benefits. Refer to the Non Interest Expenses discussion below for additional information.

For the first quarter of 2011, the Corporation recorded an income tax expense of \$3.6 million, compared to an income tax expense of \$6.9 million for the same period in 2010. The income tax expense for 2011 is mainly related to a net reduction of \$2.0 million of the Corporation's deferred tax assets associated with a reduction in statutory tax rates. Refer to the Income Taxes discussion below for additional information.

Total assets as of March 31, 2011 amounted to \$15.1 billion, down \$489.0 million from \$15.6 billion as of December 31, 2010. The Corporation continued to execute deleveraging initiatives and total loans decreased by \$560.9 million due to loan sales completed in the first quarter of 2011. Total investment securities decreased by \$430.5 million mainly due to sale and prepayments of U.S. agency MBS. Partially offsetting these decreases was an increase of \$503.0 million in cash and cash equivalent related to proceeds received from sales of loans and investments. Refer to the Financial Condition and Operating Data discussion below for additional information.

As of March 31, 2011, total liabilities amounted to \$14.1 billion, a decrease of \$458.3 million when compared to the balance as of December 31, 2010. The decrease is mainly attributable to a decrease of \$538.1 million in brokered deposits, and a \$113.0 million decrease in advances from FHLB, partially offset by an increase in core deposits of \$177.2 million and an increase of \$18.2 million in public funds. Refer to the Risk Management Liquidity and Capital Adequacy discussion below for additional information about the Corporation's funding sources.

The Corporation's stockholders' equity amounted to \$1.0 billion as of March 31, 2011, a decrease of \$30.7 million compared to the balance as of December 31, 2010, driven by the net loss of \$28.4 million for the first quarter, as well as a decrease of \$2.3 million in accumulated other comprehensive income. Refer to the Risk Management - Capital section below for additional information, including information about the Corporation's Capital Plan execution.

Total loan production, including purchases, for the quarter ended March 31, 2011 was \$696.0 million, compared to \$637.0 million for the comparable period in 2010. The increase in loan production during 2011, as compared to the first quarter of 2010, was mainly related to the acquisition loan of \$136 million provided by the Corporation to a new joint venture for the financing of loans sold to this entity and additional disbursements of approximately \$45.7 million to the joint venture as part of a credit facility used to finance completion costs of the underlying projects under construction.

Total non-performing loans as of March 31, 2011 amounted to \$1.24 billion, a decrease of \$159.8 million when compared to the balance as of December 31, 2010. The completion of the previously reported loan sale transaction with a joint venture removed approximately \$153.6 million of non-performing loans from the balance sheet. Excluding the impact of the loan sale transaction, non-performing loans decreased by \$5.9 million, reflecting declines in commercial mortgage and consumer non-performing loans

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partially offset by increases in construction and C&I non-performing loans. Refer to the Risk Management Non-accruing and Non-performing Assets section below for additional information.

CRITICAL ACCOUNTING POLICIES AND PRACTICES

The accounting principles of the Corporation and the methods of applying these principles conform with generally accepted accounting principles in the United States (GAAP). The Corporation s critical accounting policies relate to the 1) allowance for loan and lease losses; 2) other-than-temporary impairments; 3) income taxes; 4) classification and related values of investment securities; 5) valuation of financial instruments; and 6) income recognition on loans. These critical accounting policies involve judgments, estimates and assumptions made by management that affect the amounts recorded for assets and liabilities and for contingent liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from estimates, if different assumptions or conditions prevail. Certain determinations inherently require greater reliance on the use of estimates, assumptions, and judgments and, as such, have a greater possibility of producing results that could be materially different than those originally reported.

The Corporation s critical accounting policies are described in the Management s Discussion and Analysis of Financial Condition and Results of Operations included in First BanCorp s 2010 Annual Report on Form 10-K. There have not been any material changes in the Corporation s critical accounting policies since December 31, 2010.

RESULTS OF OPERATIONS

Net Interest Income

Net interest income is the excess of interest earned by First BanCorp on its interest-earning assets over the interest incurred on its interest-bearing liabilities. First BanCorp s net interest income is subject to interest rate risk due to the re-pricing and maturity mismatch of the Corporation s assets and liabilities. Net interest income for the quarter ended March 31, 2011 was \$106.3 million compared to \$116.9 million for the comparable period in 2010. On a tax-equivalent basis and excluding the changes in the fair value of derivative instruments and unrealized gains and losses on liabilities measured at fair value, net interest income for the quarter ended March 31, 2011 was \$108.8 million compared to \$128.5 million for the comparable period of 2010.

The following tables include a detailed analysis of net interest income. Part I presents average volumes and rates on an adjusted tax-equivalent basis and Part II presents, also on an adjusted tax-equivalent basis, the extent to which changes in interest rates and changes in volume of interest-related assets and liabilities have affected the Corporation s net interest income. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in volume (changes in volume multiplied by prior period rates), and (ii) changes in rate (changes in rate multiplied by prior period volumes). Rate-volume variances (changes in rate multiplied by changes in volume) have been allocated to the changes in volume and rate based upon their respective percentage of the combined totals.

The net interest income is computed on an adjusted tax-equivalent basis and excluding: (1) the change in the fair value of derivative instruments, and (2) unrealized gains or losses on liabilities measured at fair value. For definition and reconciliation of this non-GAAP measure, refer to discussions below.

Table of Contents**Part I**

Quarter ended March 31,	Average Volume		Interest income ⁽¹⁾ / expense		Average Rate ⁽¹⁾	
	2011	2010	2011	2010	2011	2010
Dollars in thousands)						
Interest-earning assets:						
Money market and other short-term investments	\$ 488,087	\$ 904,600	\$ 309	\$ 436	0.26%	0.20%
Government obligations ⁽²⁾	1,344,053	1,283,568	6,189	8,820	1.87%	2.79%
Mortgage-backed securities	1,701,179	3,266,239	17,005	40,582	4.05%	5.04%
Corporate bonds	2,000	2,000	29	29	5.88%	5.88%
FHLB stock	51,332	68,380	713	843	5.63%	5.00%
Equity securities	24,662	1,802	1	15	0.02%	3.38%
Total investments ⁽³⁾	3,611,313	5,526,589	24,246	50,725	2.72%	3.72%
Residential mortgage loans	3,262,780	3,554,096	47,844	53,599	5.95%	6.12%
Construction loans	811,530	1,483,314	6,377	8,753	3.19%	2.39%
C&I and commercial mortgage loans	5,907,727	6,652,754	58,191	67,404	3.99%	4.11%
Finance leases	278,642	313,899	5,694	6,343	8.29%	8.20%
Consumer loans	1,411,940	1,565,404	40,520	44,820	11.64%	11.61%
Total loans ^{(4) (5)}	11,672,619	13,569,467	158,626	180,919	5.51%	5.41%
Total interest-earning assets	\$ 15,283,932	\$ 19,096,056	\$ 182,872	\$ 231,644	4.85%	4.92%
Interest-bearing liabilities:						
Brokered CDs	\$ 6,019,057	\$ 7,452,195	\$ 32,769	\$ 44,382	2.21%	2.42%
Other interest-bearing deposits	5,238,157	4,678,391	21,290	21,583	1.65%	1.87%
Loans payable		804,444		2,177		1.10%
Other borrowed funds	1,660,759	3,004,155	15,222	27,300	3.72%	3.69%
FHLB advances	576,729	971,596	4,745	7,694	3.34%	3.21%
Total interest-bearing liabilities ⁽⁶⁾	\$ 13,494,702	\$ 16,910,781	\$ 74,026	\$ 103,136	2.22%	2.47%
Net interest income			\$ 108,846	\$ 128,508		
Interest rate spread					2.63%	2.45%
Net interest margin					2.89%	2.73%

(1)

On an adjusted tax-equivalent basis. The adjusted tax-equivalent yield was estimated by dividing the interest rate spread on exempt assets by 1 less Puerto Rico statutory tax rate as adjusted for changes to enacted tax rates (30.0% for the Corporation's subsidiaries other than IBEs and 25.0% for the Corporation's IBEs in 2011; 40.95% for the Corporation's subsidiaries other than IBEs and 35.95% for the Corporation's IBEs in 2010) and adding to it the cost of interest-bearing liabilities. The tax-equivalent adjustment recognizes the income tax savings when comparing taxable and tax-exempt assets. Management believes that it is a standard practice in the banking industry to present net interest income, interest rate spread and net interest margin on a fully tax-equivalent basis. Therefore, management believes these measures provide useful information to investors by allowing them to make peer comparisons. Changes in the fair value of derivative and unrealized gains or losses on liabilities measured at fair value are excluded from interest income and interest expense because the changes in valuation do not affect interest paid or received.

- (2) Government obligations include debt issued by government sponsored agencies.
- (3) Unrealized gains and losses in available-for-sale securities are excluded from the average volumes.
- (4) Average loan balances include the average of non-performing loans.
- (5) Interest income on loans includes \$2.2 million and \$3.1 million for the first quarter of 2011 and 2010, respectively, of income from prepayment penalties and late fees related to the Corporation's loan portfolio.
- (6) Unrealized gains and losses on liabilities measured at fair value are excluded from the average volumes.

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		Quarter ended March 31, 2011 compared to 2010 Increase (decrease)	
	Volume	Due to: Rate	Total
		(In thousands)	
Interest income on interest-earning assets:			
Money market and other short-term investments	\$ (235)	\$ 108	\$ (127)
Government obligations	370	(3,001)	(2,631)
Mortgage-backed securities	(16,746)	(6,831)	(23,577)
Corporate bonds			
FHLB stock	(226)	96	(130)
Equity securities	97	(111)	(14)
Total investments	(16,740)	(9,739)	(26,479)
Residential mortgage loans	(4,302)	(1,453)	(5,755)
Construction loans	(4,669)	2,293	(2,376)
C&I and commercial mortgage loans	(7,380)	(1,833)	(9,213)
Finance leases	(722)	73	(649)
Consumer loans	(4,430)	130	(4,300)
Total loans	(21,503)	(790)	(22,293)
Total interest income	(38,243)	(10,529)	(48,772)
Interest expense on interest-bearing liabilities:			
Brokered CDs	(8,029)	(3,584)	(11,613)
Other interest-bearing deposits	2,465	(2,758)	(293)
Loan payable	(2,177)		(2,177)
Other borrowed funds	(12,347)	269	(12,078)
FHLB advances	(3,212)	263	(2,949)
Total interest expense	(23,300)	(5,810)	(29,110)
Change in net interest income	(14,943)	(4,719)	(19,662)

Portions of the Corporation's interest-earning assets, mostly investments in obligations of some U.S. Government agencies and sponsored entities, generate interest which is exempt from income tax, principally in Puerto Rico. Also, interest and gains on sales of investments held by the Corporation's international banking entities are tax-exempt under the Puerto Rico tax law, except for a temporary 5% tax rate imposed by the Puerto Rico Government on IBEs' net

income effective for years that commenced after December 31, 2008 and before January 1, 2012 (refer to the Income Taxes discussion below for additional information). To facilitate the comparison of all interest data related to these assets, the interest income has been converted to an adjusted taxable equivalent basis. The tax equivalent yield was estimated by dividing the interest rate spread on exempt assets by 1 less the Puerto Rico statutory tax rate as adjusted for changes to enacted tax rates (30.0% for the Corporation's subsidiaries other than IBEs and 25.0% for the Corporation's IBEs in 2011) and adding to it the average cost of interest-bearing liabilities. The computation considers the interest expense disallowance required by Puerto Rico tax law. Refer to the Income Taxes discussion below for additional information of the Puerto Rico tax law.

The presentation of net interest income excluding the effects of the changes in the fair value of the derivative instruments and unrealized gains or losses on liabilities measured at fair value (valuations) provides additional information about the Corporation's net interest income and facilitates comparability and analysis. The changes in the fair value of the derivative instruments and unrealized gains or losses on liabilities measured at fair value have no effect on interest due or interest earned on interest-bearing liabilities or interest-earning assets, respectively, or on interest payments exchanged with interest rate swap counterparties.

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The following table reconciles net interest income in accordance with GAAP to net interest income excluding valuations, and net interest income on an adjusted tax-equivalent basis, net interest rate spread and net interest margin on a GAAP basis to these items excluding valuations and on an adjusted tax-equivalent basis:

	Quarter Ended March 31,	
	2011	2010
Net Interest Income (in thousands)		
Interest Income GAAP	\$ 180,903	\$ 220,988
Unrealized (gain) loss on derivative instruments	(345)	744
Interest income excluding valuations	180,558	221,732
Tax-equivalent adjustment	2,314	9,912
Interest income on a tax-equivalent basis excluding valuations	182,872	231,644
Interest Expense GAAP	74,624	104,125
Unrealized (loss) gain on derivative instruments and liabilities measured at fair value	(598)	(989)
Interest expense excluding valuations	74,026	103,136
Net interest income GAAP	\$ 106,279	\$ 116,863
Net interest income excluding valuations	\$ 106,532	\$ 118,596
Net interest income on a tax-equivalent basis excluding valuations	\$ 108,846	\$ 128,508
Average Balances (in thousands)		
Loans and leases	\$ 11,672,619	\$ 13,569,467
Total securities and other short-term investments	3,611,313	5,526,589
Average Interest-Earning Assets	\$ 15,283,932	\$ 19,096,056
Average Interest-Bearing Liabilities	\$ 13,494,702	\$ 16,910,781
Average Yield/Rate		
Average yield on interest-earning assets GAAP	4.80%	4.69%
Average rate on interest-bearing liabilities GAAP	2.24%	2.50%
Net interest spread GAAP	2.56%	2.19%
Net interest margin GAAP	2.82%	2.48%

Average yield on interest-earning assets excluding valuations	4.79%	4.71%
Average rate on interest-bearing liabilities excluding valuations	2.22%	2.47%
Net interest spread excluding valuations	2.57%	2.24%
Net interest margin excluding valuations	2.83%	2.52%
Average yield on interest-earning assets on a tax-equivalent basis and excluding valuations	4.85%	4.92%
Average rate on interest-bearing liabilities excluding valuations	2.22%	2.47%
Net interest spread on a tax-equivalent basis and excluding valuations	2.63%	2.45%
Net interest margin on a tax-equivalent basis and excluding valuations	2.89%	2.73%

The following table summarizes the components of the changes in fair values of interest rate swaps and interest rate caps, which are included in interest income:

(In thousands)	Quarter Ended March	
	2011	2010
Unrealized gain (loss) on derivatives (economic undesignated hedges):		
Interest rate caps	\$ 345	\$ (731)
Interest rate swaps on loans		(13)
Net unrealized gain (loss) on derivatives (economic undesignated hedges)	\$ 345	\$ (744)

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The following table summarizes the components of the net unrealized gain and loss on derivatives (economic undesignated hedges) and net unrealized gain and loss on liabilities measured at fair value which are included in interest expense:

(In thousands)	Quarter ended March	
	2011	31, 2010
Unrealized loss on derivatives (economic undesignated hedges):		
Interest rate swaps and options on stock index deposits	\$ 5	\$ 1
Interest rate swaps and options on stock index notes	5	30
Net unrealized loss on derivatives (economic undesignated hedges)	\$ 5	\$ 31
Unrealized loss on liabilities measured at fair value:		
Unrealized loss on medium-term notes	593	958
Net unrealized loss on liabilities measured at fair value	\$ 593	\$ 958
Net unrealized loss on derivatives (economic undesignated hedges) and liabilities measured at fair value	\$ 598	\$ 989

Interest income on interest-earning assets primarily represents interest earned on loans receivable and investment securities.

Interest expense on interest-bearing liabilities primarily represents interest paid on brokered CDs, branch-based deposits, repurchase agreements, advances from the FHLB and FED and notes payable.

Unrealized gains or losses on derivatives represent changes in the fair value of derivatives, primarily interest rate swaps used for protection against rising interest rates.

Unrealized gains or losses on liabilities measured at fair value represent the change in the fair value of such liabilities (medium-term notes), other than the accrual of interests.

Derivative instruments, such as interest rate swaps, are subject to market risk. While the Corporation does have certain trading derivatives to facilitate customer transactions, the Corporation does not utilize derivative instruments for speculative purposes. As of March 31, 2011, most of the interest rate swaps outstanding are used for protection against rising interest rates. Refer to Note 9 of the accompanying unaudited consolidated financial statements for further details concerning the notional amounts of derivative instruments and additional information. As is the case with investment securities, the market value of derivative instruments 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 net interest income. 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.

Net interest income decreased 9% to \$106.3 million for the first quarter of 2011 from \$116.9 million in the first quarter of 2010. The decrease in net interest income is largely due to the decrease in volume of interest-earning assets, consistent with the Corporation's capital plan that includes deleverage initiatives to preserve and improve the Corporation's capital position. Average total loans and leases decreased 14% or \$1.9 billion mainly due to loan sales completed throughout 2010 and in the first quarter of 2011. Average investment securities and other short-term investments decreased 35% or \$1.9 billion mainly as a result of sales and prepayments of mortgage-backed securities of which proceeds have been used to pay-down high cost interest borrowings such as repurchase agreements and

brokered CDs. The Corporation has sold approximately \$2.3 billion of investment securities over the last 12 months, mainly U.S. agency MBS, including the sale during the first quarter of 2011 of approximately \$330 million of U.S. agency MBS originally intended to be held to maturity.

The average volume of all major loan categories, in particular the average volume of construction and commercial loans, decreased when compared to the first quarter of 2010. The decrease of \$671.8 million in the average volume of construction loans is primarily related to sales of performing and non-performing loans completed over the last 12 months, including construction loans with a book value of \$201.5 million sold in the first quarter of 2011 as part of the aforementioned loan sale transaction with the joint venture. Before charge-offs recorded at the time of the transfer of loans to held for sale in the fourth quarter of 2010, the carrying value of such construction loans sold to the joint venture amounted to \$325.4 million. Other reductions came from charge-off activity, repayments and sales of non-performing credits in Florida in 2010. Average C&I and commercial mortgage loans decreased by \$745.0 million primarily related to both paydowns and charge-offs, including repayments of facilities granted to the Puerto Rico and Virgin Islands governments, and loans sold. The average volume of residential mortgage loans decreased by \$291.3 million primarily related to sales of performing loans, including \$236 million of performing residential mortgage loans sold to another financial institution in the first

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quarter of 2011, pay-downs and charge-off activity. The average volume of consumer loans, including finance leases, decreased by \$188.7 million, resulting from paydowns and charge-offs that exceeded new loan originations.

Partially offsetting the decline in the average volume of earning assets was an increase of 16 basis points in the net interest margin (on a tax equivalent basis), reflecting the positive impacts of an increase in core deposits at a lower cost coupled with benefits from the roll-off and repayments of higher cost funds, such as maturing brokered CDs, and the stabilization of non-performing loan levels. The overall average cost of funding decreased 25 basis points in the first quarter of 2011 when compared to the same period in 2010. These favorable factors were partially offset by lower yields on MBS. The average balance of interest bearing non-brokered deposits increased \$559.8 million while the average balance of brokered CDs decreased by \$1.4 billion.

On an adjusted tax-equivalent basis, net interest income decreased by \$19.7 million, or 15%, for the first quarter of 2011 compared to the same period in 2010. The decrease for the first quarter of 2011, as compared to the corresponding period of 2010, was principally due to a decrease in average interest earning assets, as discussed above, while the tax-equivalent adjustment decreased by \$7.6 million. The tax-equivalent adjustment increases interest income on tax-exempt securities and loans by an amount which makes tax-exempt income comparable, on a pre-tax basis, to the Corporation's taxable income as previously stated. The decrease in the tax-equivalent adjustment was mainly related to decreases in tax-exempt assets, lower yields on U.S. agency and MBS held by the Bank's IBE subsidiary, and due to the reduction in the statutory tax rates.

Provision and Allowance for Loan and Lease Losses

The provision for loan and lease losses is charged to earnings to maintain the allowance for loan and lease losses at a level that the Corporation considers adequate to absorb probable losses inherent in the portfolio. The adequacy of the allowance for loan and lease losses is also based upon a number of additional factors including trends in charge-offs and delinquencies, current economic conditions, the fair value of the underlying collateral and the financial condition of the borrowers, and, as such, includes amounts based on judgments and estimates made by the Corporation. Although the Corporation believes that the allowance for loan and lease losses is adequate, factors beyond the Corporation's control, including factors affecting the economies of Puerto Rico, the United States, the U.S. Virgin Islands and the British Virgin Islands, may contribute to delinquencies and defaults, thus necessitating additional reserves.

For the quarter ended on March 31, 2011, the Corporation recorded a provision for loan and lease losses of \$88.7 million compared to \$171.0 million for the comparable period in 2010. The decrease was mainly related to a \$76.8 million decrease in the provision for construction loans due to lower charge-offs driven by stabilization in property values and the reduction in the concentration of residential construction loans. Additionally, a decrease in inflows of construction loans to non-accrual status and a decrease in the level of adversely classified loans, which require higher reserves, contributed to a lower provision. Total adversely classified construction loans decreased \$481.4 million, or 54%, over the last 12 months. The decrease in adversely classified loans is a result of the execution of several initiatives to accelerate the de-risking of the balance sheet, including the aforementioned loan portfolio sale to a joint venture.

The provision for commercial mortgage loans decreased by \$24.2 million primarily driven by a decrease in non-performing loans. The provision for residential mortgage loans decreased by \$22.4 million driven by improvements in delinquency and charge-off trends and the provision for consumer loans, including finance leases, decreased by \$8.0 million primarily related to improvements in charge-off trends and economic factors. Partially offsetting the aforementioned decreases was a \$49.2 million increase in the provision for C&I loans driven by an increase in non-performing loans.

In terms of geography, the Corporation recorded a provision of \$57.0 million in the first quarter of 2011 for its loan portfolio in Puerto Rico compared to \$88.0 million in the comparable 2010 quarter, a decrease of \$31.0 million. The decrease is mainly related to the construction and residential mortgage loan portfolio. The provision for construction loans in Puerto Rico decreased by \$54.2 million mainly due to reductions in charge-offs, non-performing and adversely classified loans as mentioned above. The provision for residential mortgage loans decreased by \$15.3 million due to improvements in delinquency and charge-off trends, while the provision for consumer loans, including finance leases decreased by \$7.3 million. The provision for commercial mortgage loans in Puerto Rico

decreased by \$1.0 million due to a reduction in non-performing and adversely classified loans. The aforementioned decreases in the provision were partially offset by an increase of \$46.9 million in the provision for C&I loans mainly due to an increase in the migration of loans to non-accrual status.

With respect to the loan portfolio in the United States, the Corporation recorded a \$7.9 million provision for the first quarter of 2011 compared to a \$71.2 million provision for the first quarter of 2010. The decrease of \$63.3 million is mainly related to the construction and commercial mortgage loan portfolios. The provision for construction loans in the United States decreased by \$35.2 million compared to the first quarter of 2010, primarily due to decreases to specific reserves, as a result of sales of non-performing loans throughout 2010, the slower migration of loans to non-performing status and the overall reduction of the Corporation's exposure to construction loans in Florida to \$70.4 million, compared to an exposure of \$277.6 million a year ago. The provision for commercial mortgage loans in the United States decreased by \$23.2 million compared to the first quarter of 2010 also due to lower charges to specific reserves and a slower migration of

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loans to non-accrual status. The provision for residential mortgage loans decreased by \$6.0 million, while the provision for C&I loans in the United States portfolio increased slightly by \$1.3 million.

The provision recorded for the loan portfolio in the Virgin Islands amounted to \$23.8 million in the first quarter of 2011, an increase of \$12.0 million compared to the same period a year ago mainly associated with the construction loan portfolio. The provision for construction loans increased by \$12.5 million substantially related to one relationship amounting to \$100 million which was placed in non-accrual status. Refer to the discussions under **Credit Risk Management** below for an analysis of the allowance for loan and lease losses, non-performing assets, impaired loans and related information and refer to the discussions under **Financial Condition and Operating Analysis** **Loan Portfolio** and under **Risk Management** **Credit Risk Management** below for additional information concerning the Corporation's loan portfolio exposure in the geographic areas where the Corporation does business.

Non-Interest Income

	Quarter Ended March 31,	
	2011	2010
	(In thousands)	
Other service charges on loans	\$ 1,718	\$ 1,756
Service charges on deposit accounts	3,332	3,468
Mortgage banking activities	6,591	2,500
Insurance income	1,333	2,275
Broker-dealer income	48	207
Other operating income	8,122	4,356
Non-interest income before net gain on investments	21,144	14,562
Proceeds from securities litigation settlement	631	
Gain on VISA shares and related proceeds		10,668
Net gain on sale of investments	18,710	20,696
OTTI on equity securities		(600)
Net gain on investments	19,341	30,764
Total	\$ 40,485	\$ 45,326

Non-interest income primarily consists of other service charges on loans; service charges on deposit accounts; commissions derived from various banking, securities and insurance activities; gains and losses on mortgage banking activities; and net gains and losses on investments and impairments.

Other service charges on loans consist mainly of service charges on credit card-related activities and other non-deferrable fees (e.g. agent, commitment and drawing fees).

Service charges on deposit accounts include monthly fees and other fees on deposit accounts.

Income from mortgage banking activities includes gains on sales and securitization of loans and revenues earned for administering residential mortgage loans originated by the Corporation and subsequently sold with servicing retained. In addition, lower-of-cost-or-market valuation adjustments to the Corporation's residential mortgage loans held for sale portfolio and servicing rights portfolio, if any, are recorded as part of mortgage banking activities.

Insurance income consists of insurance commissions earned by the Corporation's subsidiary, FirstBank Insurance Agency, Inc., and the Bank's subsidiary in the U.S. Virgin Islands, FirstBank Insurance V.I., Inc. These subsidiaries offer a wide variety of insurance business.

The other operating income category is composed of miscellaneous fees such as debit, credit card and point of sale (POS) interchange fees and check and cash management fees and includes commissions from the Corporation's broker-dealer subsidiary, FirstBank Puerto Rico Securities.

The net gain (loss) on investment securities reflects gains or losses as a result of sales that are consistent with the Corporation's investment policies as well as OTTI charges on the Corporation's investment portfolio.

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Non-interest income decreased \$4.8 million to \$40.5 million for the first quarter of 2011 from \$45.3 million for the first quarter of 2010. The decrease in non-interest income was primarily a result of a decrease in gains from sales of investments primarily due to a \$10.7 million gain on the sale of VISA Class C shares recognized in the first quarter of 2010 and a reduction of \$2.0 million in gains on sale of MBS due to a lower volume of sales. Some of the most significant transactions that affected non-interest income during the first quarter of 2011 follow:

An \$18.7 million gain on the sale of approximately \$330 million of FNMA MBS as part of the Corporation's deleverage strategies. There were also proceeds of approximately \$0.6 million in the first quarter of 2011 from a securities litigation settlement.

A \$5.3 million gain on the bulk sale of \$236 million of performing residential mortgage loans to another financial institution.

A \$2.8 million gain on substantially all of the assets of FirstBank Insurance Agency VI. This transaction represents a repositioning of the Bank's insurance business in the Virgin Islands to bring it more in line with its Puerto Rico insurance business model.

Non-Interest Expenses

The following table presents the detail of non-interest expenses for the periods indicated:

	Quarter Ended March 31,	
	2011	2010
	(In thousands)	
Employees' compensation and benefits	\$ 30,439	\$ 31,728
Occupancy and equipment	15,250	14,851
Deposit insurance premium	13,465	16,653
Other taxes, insurance and supervisory fees	4,967	5,686
Professional fees - recurring	4,180	4,529
Professional fees - non-recurring	957	758
Servicing and processing fees	2,211	2,008
Business promotion	2,664	2,205
Communications	1,878	2,114
Net loss on REO operations	5,500	3,693
Other	1,355	7,137
	\$ 82,866	\$ 91,362

Non-interest expenses decreased \$8.5 million to \$82.9 million for the first quarter of 2011 from \$91.4 million for the first quarter of 2010. The decrease reflected:

A decrease of \$3.2 million in the FDIC deposit insurance premium primarily related to a decrease in average deposits (mainly in brokered CDs).

A \$6.6 million decrease in the provision for off-balance sheet exposures due to reductions in letters of credit and unfunded loan commitment balances.

A \$1.3 million decrease in employee compensation and benefits as a result of cost reduction strategies implemented during 2010 and reductions in headcount. Over the last 12 months, the Corporation reduced its headcount by approximately 138 or 5%.

The aforementioned decreases were partially offset by a \$1.8 million increase in foreclosure-related expenses mainly due to higher write-downs to the value of repossessed properties and costs associated with a higher inventory.

Income Taxes

Income tax expense includes Puerto Rico and Virgin Islands income taxes as well as applicable U.S. federal and state taxes. The Corporation is subject to Puerto Rico income tax on its income from all sources. As a Puerto Rico corporation, First BanCorp is treated as a foreign corporation for U.S. income tax purposes and is generally subject to United States income tax only on its income from sources within the United States or income effectively connected with the conduct of a trade or business within the United States. Any such tax paid is creditable, within certain conditions and limitations, against the Corporation's Puerto Rico tax liability. The Corporation is also subject to U.S. Virgin Islands taxes on its income from sources within that jurisdiction. Any such tax paid is also creditable against the Corporation's Puerto Rico tax liability, subject to certain conditions and limitations.

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Under the Puerto Rico Internal Revenue Code of 1994, as amended (the PR Code), the Corporation and its subsidiaries are treated as separate taxable entities and are not entitled to file consolidated tax returns and, thus, the Corporation is not able to utilize losses from one subsidiary to offset gains in another subsidiary. Accordingly, in order to obtain a tax benefit from a net operating loss, a particular subsidiary must be able to demonstrate sufficient taxable income within the applicable carry forward period (7 years under the PR Code). The PR Code provides a dividend received deduction of 100% on dividends received from controlled subsidiaries subject to taxation in Puerto Rico and 85% on dividends received from other taxable domestic corporations. Dividend payments from a U.S. subsidiary to the Corporation are subject to a 10% withholding tax based on the provisions of the U.S. Internal Revenue Code.

Under the PR Code, First BanCorp is subject to a maximum statutory tax rate of 39%. In 2009 the Puerto Rico Government approved Act No. 7 (the Act), to stimulate Puerto Rico's economy and to reduce the Puerto Rico Government's fiscal deficit. The Act imposes a series of temporary and permanent measures, including the imposition of a 5% surtax over the total income tax determined, which is applicable to corporations, among others, whose combined income exceeds \$100,000, effectively resulting in an increase in the maximum statutory tax rate from 39% to 40.95% and an increase in the capital gain statutory tax rate from 15% to 15.75%. These temporary measures are effective for tax years that commenced after December 31, 2008 and before January 1, 2012. The PR Code also includes an alternative minimum tax of 22% that applies if the Corporation's regular income tax liability is less than the alternative minimum tax requirements.

The Corporation has maintained an effective tax rate lower than the maximum statutory rate mainly by investing in government obligations and mortgage-backed securities exempt from U.S. and Puerto Rico income taxes and by doing business through International Banking Entity (IBE) of the Bank (FirstBank IBE) and through the Bank's subsidiary, FirstBank Overseas Corporation, in which the interest income and gain on sales is exempt from Puerto Rico and U.S. income taxation. Under the Act, all IBE are subject to the special 5% tax on their net income not otherwise subject to tax pursuant to the PR Code. This temporary measure is also effective for tax years that commenced after December 31, 2008 and before January 1, 2012. FirstBank IBE and FirstBank Overseas Corporation were created under the International Banking Entity Act of Puerto Rico, which provides for total Puerto Rico tax exemption on net income derived by IBEs operating in Puerto Rico. IBEs that operate as a unit of a bank pay income taxes at normal rates to the extent that the IBEs' net income exceeds 20% of the bank's total net taxable income.

On January 31, 2011, the Puerto Rico Government approved Act No. 1, which repealed the 1994 PR Code and replaces it with the Puerto Rico Internal Revenue Code of 2010 (the 2010 PR Code). The provisions of the 2010 Code are generally applicable to taxable years commencing after December 31, 2010. The matters discussed above are equally applicable under the 2010 Code except that the maximum corporate tax rate has been reduced from 39% (40.95% for calendar years 2009 and 2010) to 30% (25% for taxable years commencing after December 31, 2013 if certain economic conditions are met by the Puerto Rico economy). Corporations are entitled to elect continue to determine its Puerto Rico income tax responsibility for such 5 year period under the provisions of the 1994 Code.

For the quarter ended March 31, 2011, the Corporation recorded an income tax expense of \$3.6 million compared to an income tax expense of \$6.9 million for the same period in 2010. As a result of the reduction in the statutory income tax rates from 39% to 30% under the new 2010 Code, the Corporation recorded a \$102.0 million reduction in its deferred tax assets and a \$100.0 million reduction in the valuation allowance. Since the majority of the deferred tax assets were reserved prior to 2011, the net charge to the income statement during the first quarter of 2011 attributed to changes in tax rates was approximately \$2.0 million in connection with profitable subsidiaries. As of March 31, 2011, the deferred tax asset, net of a valuation allowance of \$355.4 million, amounted to \$7.7 million compared to \$9.3 million as of December 31, 2010. The Corporation continued to reserve deferred tax assets created in connection with the operations of its banking subsidiary, FirstBank.

Accounting for income taxes requires that companies assess whether a valuation allowance should be recorded against their deferred tax asset based on the consideration of all available evidence, using a more likely than not realization standard. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount that is more likely than not to be realized. In making such assessment, significant weight is to be given to evidence that can be objectively verified, including both positive and negative evidence. The accounting for income taxes

guidance requires the consideration of all sources of taxable income available to realize the deferred tax asset, including the future reversal of existing temporary differences, future taxable income exclusive of the reversal of temporary differences and carryforwards, taxable income in carryback years and tax planning strategies. In estimating taxes, management assesses the relative merits and risks of the appropriate tax treatment of transactions taking into account statutory, judicial and regulatory guidance, and recognizes tax benefits only when deemed probable of realization.

In assessing the weight of positive and negative evidence, a significant negative factor that resulted in increases of the valuation allowance was that the Corporation's banking subsidiary, FirstBank Puerto Rico, continues in a three-year historical cumulative loss position as of the end of the first quarter of 2011, and has projected to be in a loss position for the remaining of 2011. As of March 31, 2011, management concluded that \$7.7 million of the deferred tax asset will be realized. The Corporation's deferred tax assets for which it has not established a valuation allowance relate to profitable subsidiaries and to amounts that can be realized through future reversals of existing taxable temporary differences. To the extent the realization of a portion, or all, of the tax asset becomes more

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likely than not based on changes in circumstances (such as, improved earnings, changes in tax laws or other relevant changes), a reversal of that portion of the deferred tax asset valuation allowance will then be recorded.

The tax effect of the unrealized holding gain or loss on securities available-for-sale, excluding that on securities held by the Corporation's international banking entities which is exempt, was computed based on a 15% capital gain tax rate, and is included in accumulated other comprehensive income as part of stockholders' equity.

The FASB guidance prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of income tax uncertainties with respect to positions taken or expected to be taken on income tax returns. Under the authoritative accounting guidance, income tax benefits are recognized and measured based upon a two-step model: 1) a tax position must be more likely than not to be sustained based solely on its technical merits in order to be recognized, and 2) the benefit is measured as the largest dollar amount of that position that is more likely than not to be sustained upon settlement. The difference between the benefit recognized in accordance with this model and the tax benefit claimed on a tax return is referred to as an UTB.

The Corporation classified all interest and penalties, if any, related to tax uncertainties as income tax expense. The amount of UTBs may increase or decrease for various reasons, including changes in the amounts for current tax year positions, the expiration of open income tax returns due to the expiration of statutes of limitations, changes in management's judgment about the level of uncertainty, the status of examinations, litigation and legislative activity and the addition or elimination of uncertain tax positions. There were no UTBs outstanding as of March 31, 2011 and December 31, 2010.

FINANCIAL CONDITION AND OPERATING DATA ANALYSIS**Assets**

Total assets were approximately \$15.1 billion as of March 31, 2011, down \$489.0 million from approximately \$15.6 billion as of December 31, 2010. The Corporation continued with the execution of deleverage initiatives included in its Capital Plan. Total loans decreased by \$560.9 million driven by the completion of the sale of loans with an approximate book value of \$269.3 million to a joint venture and the bulk sale of approximately \$236 million of residential mortgage loans to another financial institution. Total investment securities decreased by \$430.5 million mainly due to the sale and prepayments of U.S. agency MBS, including the sale of \$330 million of MBS originally intended to be held to maturity, consistent with the deleveraging initiatives included in the Corporation's Capital Plan. After the sale, in line with the Corporation's ongoing capital management strategy, the remaining \$89 million of investment securities held in the held-to-maturity portfolio were reclassified to the available-for-sale portfolio during the first quarter of 2011. Also, U.S. agency debt securities of approximately \$50 million were called prior to their contractual maturities during the first quarter of 2011. Proceeds from sales of loans and investments, and the increase in core deposits, contributed to the increase of \$503.0 million in cash and cash equivalents that strengthened the liquidity reserves. Such excess liquidity is expected to be used, in part, to pay down brokered CDs maturing during the second quarter of 2011. Refer to the Loan portfolio and Investment Activities discussion below for additional information.

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The following table presents the composition of the Corporation's loan portfolio, including loans held for sale, as of the dates indicated:

<i>(In thousands)</i>	March 31, 2011	December 31, 2010
Residential mortgage loans	\$ 2,896,692	\$ 3,417,417
Commercial loans:		
Commercial mortgage loans	1,588,768	1,670,161
Construction loans	682,245	700,579
Commercial and Industrial loans	3,977,301	3,861,545
Loans to local financial institutions collateralized by real estate mortgages	285,359	290,219
Total commercial loans	6,533,673	6,522,504
Finance leases	272,392	282,904
Consumer loans and other loans	1,387,018	1,432,611
Total loans held for investment	11,089,775	11,655,436
Loans held for sale	305,494	300,766
	11,395,269	11,956,202
Less:		
Allowance for loan and lease losses	(561,695)	(553,025)
Total loans, net	\$ 10,833,574	\$ 11,403,177

As of March 31, 2011, the Corporation's total loans decreased by \$569.6 million, when compared with the balance as of December 31, 2010. All major loan categories decreased from 2010 levels mainly as a result of loan sales coupled with pay-downs and charge-offs, with the exception of C&I loans which increased due to loans granted in relation to the loan sale transaction with the joint venture.

Of the total gross loan portfolio held for investment of \$11.1 billion as of March 31, 2011, approximately 83% have credit risk concentration in Puerto Rico, 8% in the United States (mainly in the state of Florida) and 9% in the Virgin Islands, as shown in the following table:

As of March 31, 2011	Puerto Rico	Virgin Islands	United States	Total
	(In thousands)			
Residential mortgage loans	\$ 2,147,770	\$ 426,530	\$ 322,392	\$ 2,896,692

Commercial loans:				
Commercial mortgage loans	1,063,541	66,975	458,252	1,588,768
Construction loans	423,800	188,027	70,418	682,245
Commercial and Industrial loans	3,750,455	198,457	28,389	3,977,301
Loans to a local financial institution collateralized by real estate mortgages	285,359			285,359
Total commercial loans	5,523,155	453,459	557,059	6,533,673
Finance leases	272,392			272,392
Consumer loans	1,289,627	66,615	30,776	1,387,018
Total loans held for investment, gross	9,232,944	946,604	910,227	11,089,775
Allowance for loan and lease losses	(431,814)	(69,797)	(60,084)	(561,695)
Total loans held for investment, net	8,801,130	876,807	850,143	10,528,080
Loans held for sale	299,493	6,001		305,494
	\$ 9,100,623	\$ 882,808	\$ 850,143	\$ 10,833,574

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First BanCorp relies primarily on its retail network of branches to originate residential and consumer loans. The Corporation supplements its residential mortgage originations with wholesale servicing released mortgage loan purchases from mortgage bankers. The Corporation manages its construction and commercial loan originations through centralized units and most of its originations come from existing customers as well as through referrals and direct solicitations.

The following table details First BanCorp's loan production, including purchases and refinancing, for the periods indicated:

	Quarter Ended March 31,	
	2011	2010
	(In thousands)	
Residential real-estate	\$ 115,226	\$ 126,672
C&I and commercial mortgage	419,023	304,935
Construction	35,357	50,853
Finance leases	20,110	23,050
Consumer	106,290	131,483
Total loan production	\$ 696,006	\$ 636,993

The Corporation is experiencing continued loan demand and has continued with its targeted origination strategies. Total loan originations for the first quarter of 2011, including refinancing and draws from existing commitments, amounted to approximately \$696.0 million, an increase of \$59.0 million when compared to the same period in 2010. The increase is primarily related to a \$114.1 million increase in commercial loan originations, which include the acquisition loan of \$136 million provided by FirstBank to the joint venture for the financing of the loans sold and additional disbursements of approximately \$45.7 million to the joint venture as part of a credit facility used to finance completion costs of the underlying projects under construction. The remaining portfolios reflected decreases in originations. Residential mortgage loan originations, including purchases of \$35.6 million, amounted to \$115.2 million, down from \$126.7 million in the first quarter of 2010. Consumer loan originations amounted to \$106.3 million, down from \$131.5 million for the same quarter in 2010. Credit facilities granted to government were \$21.6 million for the first quarter of 2011 compared to \$76 million for the first quarter of 2010.

Residential Real Estate Loans

As of March 31, 2011, the Corporation's residential real estate loan portfolio held for investment decreased by \$520.7 million as compared to the balance as of December 31, 2010. The majority of the Corporation's outstanding balance of residential mortgage loans consists of fixed-rate, fully amortizing, full documentation loans. In accordance with the Corporation's underwriting guidelines, residential real estate loans are mostly fully documented loans, and the Corporation is not actively involved in the origination of negative amortization loans or adjustable-rate mortgage loans. The decrease was mainly attributed to a combination of sales of \$236 million of loans to another financial institution, sales of \$20.7 million to FNMA and FHLMC in the secondary market, and securitizations amounting to \$41.5 million. Also, during the first quarter of 2011 the Corporation reclassified approximately \$282 million of residential mortgage loans held for investment to held for sale, pursuant to a letter of intent to sell loans entered into by FirstBank with another financial institution. These loans were subsequently sold in April of 2011. Refer to the Contractual Obligations and Commitments discussion below for additional information about outstanding commitments to sell mortgage loans.

Commercial and Construction Loans

As of March 31, 2011, the Corporation's commercial and construction loan portfolio held for investment increased by \$11.2 million, as compared to the balance as of December 31, 2010, due mainly to \$181.7 million in loans granted to the joint venture as part of the loan sale transaction, partially offset by \$64.6 million in charge-offs, pay downs and loans foreclosed. The Corporation's commercial loans are primarily variable- and adjustable-rate loans.

On February 16, 2011, the Corporation sold an asset portfolio consisting on performing and non-performing construction, commercial mortgage and C&I loans with an aggregate book value of \$269.3 million to a new joint venture (the Joint Venture) organized under the Laws of the Commonwealth of Puerto Rico and majority owned by PRLP Ventures LLC (PRLP), a company created by Goldman, Sachs & Co. and Caribbean Property Group (CPG). In exchange for the sale, the Corporation received \$88.5 million in cash; a 35% interest in the Joint Venture, valued at \$47.6 million; and \$136.1 million representing seller financing provided by FirstBank, which has a 7-year maturity and bears variable interest at 30-day LIBOR plus 300 basis points and is secured by a pledge of all of the acquiring entity s assets as well as the PRLP s 65% ownership interest in the Joint Venture. As of March 31, 2011, the carrying amount of the loan is \$136.1 million and is included in the Corporation s C&I loan receivable portfolio; while the carrying value of FirstBank s equity interest is \$47.6 million as of March 31, 2011 and is included as part of Other Equity Securities in the Statement of Financial Condition.

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FirstBank will additionally provide an \$80 million advance facility to the Joint Venture to fund unfunded commitments and costs to complete projects under construction, of which \$45.7 million were disbursed in the first quarter of 2011, and a \$20 million working capital line of credit to fund certain expenses of the Joint Venture. These loans will bear variable interest at 30-day LIBOR plus 300 basis points. As of March 31, 2011, the carrying value of the advance facility and working capital line were \$45.7 million and \$0, respectively, and are included in the Corporation's C&I loan receivable portfolio.

As of March 31, 2011, the Corporation had \$325.9 million outstanding of credit facilities granted to the Puerto Rico Government and/or its political subdivisions, up from \$325.1 million as of December 31, 2010, and \$98.8 million granted to the Virgin Islands government, up from \$84.3 million as of December 31, 2010. A substantial portion of these credit facilities are obligations that have a specific source of income or revenues identified for their repayment, such as property taxes collected by the central Government and/or municipalities. Another portion of these obligations consists of loans to public corporations that obtain revenues from rates charged for services or products, such as electric power and water utilities. Public corporations have varying degrees of independence from the central Government and many receive appropriations or other payments from it. The Corporation also has loans to various municipalities in Puerto Rico for which the good faith, credit and unlimited taxing power of the applicable municipality have been pledged to their repayment.

Aside from loans extended to the Puerto Rico and its political subdivision, the largest loan to one borrower as of March 31, 2011 in the amount of \$285.4 million is with one mortgage originator in Puerto Rico, Doral Financial Corporation. This commercial loan is secured by individual real-estate loans, mostly 1-4 residential mortgage loans.

Construction loans originations decreased by \$15.5 million due to the strategic decision by the Corporation to reduce its exposure to construction projects in both Puerto Rico and the United States. The Corporation's construction lending volume has been stagnant for the last two years due to the slowdown in the U.S. housing market and the current economic environment in Puerto Rico. The Corporation has reduced its exposure to condo-conversion loans in its Florida operations and construction loan originations in Puerto Rico are mainly draws from existing commitments. Approximately 875 residential housing units, or 4% of the total housing inventory available in the Puerto Rico market, are residential projects financed by the Corporation, of which approximately 687 are units with sales prices under \$200,000. More than 95% of the construction loan originations in 2011 are related to disbursements from previous established commitments and new loans are mainly associated with construction loans to individuals. In Puerto Rico, absorption rates on low income residential projects financed by the Corporation showed signs of improvement during 2010 but the market is still under pressure because of an oversupply of housing units compounded by lower demand and diminished consumer purchasing power and confidence.

As a key initiative to increase the absorption rate in residential construction projects, the Corporation has engaged in discussions with developers to review sales strategies and provide additional incentives to supplement the Puerto Rico Government housing stimulus package enacted in September 2010. From September 1, 2010 to June 30, 2011, the Government of Puerto Rico is providing tax and transaction fees incentives to both purchasers and sellers (whether a Puerto Rico resident or not) of new and existing residential property, as well as commercial property with a sales price of no more than \$3 million. Among its provisions, the housing stimulus package provides various types of income and property taxes exemptions as well as reduced closing costs, including:

§ Purchase/Sale of New Residential Property within the Period

- Any long term capital gain upon selling new residential property will be 100% exempt from the payment of income taxes. The purchaser will have an exemption for five years on the payment of property taxes. The cost of filing stamps and seals are waived during the period.

§ Purchase/Sale of Existing Residential Property, or Commercial Property with a Sales Price of No More than \$3 Million, within the Period (Qualified Property)

- Any long term capital gain upon selling Qualified Property within the Period will be 100% exempt from the payment of income taxes. Fifty percent of the long term capital gain derived from the future sale of the foregoing property will be exempt from the payment of income taxes, including the basic alternative tax and the alternative minimum tax. Fifty percent of the cost of filing stamps and seals are waived during the period.

§ Rental Income from Residential Properties

- Income derived from the rental of new or existing residential property will be exempt from income taxes for a period of up to 10 calendar years, commencing on January 1, 2011.

This legislation is aimed to alleviate some of the stress in the construction industry.

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The construction loan portfolio held for investment in Puerto Rico decreased by \$13.5 million during the first quarter of 2011 driven mainly by charge-offs. In Florida the construction portfolio decreased by \$8.1 million, also driven by charge-offs during the first quarter of 2011.

The composition of the Corporation's construction loan portfolio held for investment as of March 31, 2011 by category and geographic location follows:

As of March 31, 2011	Puerto Rico	Virgin Islands	Florida	Total
	(In thousands)			
Loans for residential housing projects:				
High-rise ⁽¹⁾	\$ 16,590	\$	\$	\$ 16,590
Mid-rise ⁽²⁾	34,021	4,939	15,159	54,119
Single-family detach	51,208	9,620	9,049	69,877
Total for residential housing projects	101,819	14,559	24,208	140,586
Construction loans to individuals secured by residential properties	12,182	10,076		22,258
Condo-conversion loans	7,619			7,619
Loans for commercial projects	140,392	120,078		260,470
Bridge loans residential	57,133			57,133
Bridge loans commercial		24,032	12,997	37,029
Land loans residential	54,256	16,497	22,550	93,303
Land loans commercial	48,380	2,126	10,679	61,185
Working capital	3,078	1,041		4,119
Total before net deferred fees and allowance for loan losses	424,859	188,409	70,434	683,702
Net deferred fees	(1,059)	(382)	(16)	(1,457)
Total construction loan portfolio, gross	423,800	188,027	70,418	682,245
Allowance for loan losses	(82,675)	(57,624)	(16,898)	(157,197)
Total construction loan portfolio, net	\$ 341,125	\$ 130,403	\$ 53,520	\$ 525,048

(1) For purposes of the above table, high-rise portfolio is composed of buildings with more than 7 stories, composed of two projects in Puerto Rico.

(2) Mid-rise relates to buildings of up to 7 stories.

The following table presents further information on the Corporation's construction portfolio as of and for the quarter ended March 31, 2011:

(Dollars in thousands)

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Total undisbursed funds under existing commitments	\$	155,783
Construction loans held for investment in non-accrual status ⁽¹⁾	\$	341,179
Net charge offs Construction loans ⁽²⁾	\$	17,238
Allowance for loan losses Construction loans	\$	157,197
Non-performing construction loans to total construction loans		50.01%
Allowance for loan losses construction loans to total construction loans		23.04%
Net charge-offs (annualized) to total average construction loans ⁽²⁾		8.50%

(1) Excludes \$5.5 million of non-performing construction loans held for sale as of March 31, 2011.

(2) Includes charge-offs of \$5.2 million related to construction loans in Florida and \$12.0 million related to construction loans in Puerto Rico.

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The following summarizes the construction loans for residential housing projects in Puerto Rico segregated by the estimated selling price of the units:

(In thousands)	
Under \$300k	\$ 63,289
\$300k - \$600k	11,120
Over \$600k (1)	27,410
	\$ 101,819

(1) Mainly composed of one single-family detached projects that account for approximately 71% of the residential housing projects in Puerto Rico with selling prices over \$600k.

Consumer Loans and Finance Leases

As of March 31, 2011, the Corporation's consumer loan and finance leases portfolio decreased by \$56.1 million, as compared to the portfolio balance as of December 31, 2010. This is mainly the result of repayments and charge-offs that on a combined basis more than offset the volume of loan originations during the first quarter of 2011.

Nevertheless, the Corporation experienced a decrease in net charge-offs for consumer loans and finance leases that amounted to \$10.3 million for the first quarter of 2011, as compared to \$14.1 million for the same period a year ago.

Investment Activities

As part of its strategy to diversify its revenue sources and maximize its net interest income, First BanCorp maintains an investment portfolio that is classified as available-for-sale or held-to-maturity. The Corporation's total investment securities portfolio as of March 31, 2011 aggregated \$2.8 billion, a reduction of \$430.5 million mainly due to the sale and prepayments of U.S. agency MBS, including the sale of \$330 million of MBS originally intended to be held to maturity in line with the deleverage initiatives included in the Corporation's Capital Plan. After the sale and consistent with the Corporation's ongoing capital management strategy, the remaining \$89 million of investment securities held in the held-to-maturity portfolio were reclassified to the available-for-sale portfolio during the first quarter of 2011. Also, U.S. agency debt securities of approximately \$50 million were called prior to its contractual maturity during the first quarter of 2011.

Over 91% of the Corporation's available-for-sale and held-to-maturity securities portfolio is invested in U.S. Government and Agency debentures and fixed-rate U.S. government sponsored-agency MBS (mainly GNMA, FNMA and FHLMC fixed-rate securities). The Corporation's investment in equity securities classified as available for sale is minimal, approximately \$0.1 million, which consists of common stock of another financial institution in Puerto Rico.

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The following table presents the carrying value of investments at the indicated dates:

<i>(In thousands)</i>	As of March 31, 2011	As of December 31, 2010
	(In thousands)	
Money market investments	\$ 209,713	\$ 115,560
Investment securities held-to-maturity, at amortized cost:		
U.S. Government and agencies obligations		8,487
Puerto Rico Government obligations		23,949
Mortgage-backed securities		418,951
Corporate bonds		2,000
		453,387
Investment securities available-for-sale, at fair value:		
U.S. Government and agencies obligations	1,167,486	1,212,067
Puerto Rico Government obligations	161,854	136,841
Mortgage-backed securities	1,393,485	1,395,486
Corporate bonds	1,295	
Equity securities	47	59
	2,724,167	2,744,453
Other equity securities, including \$50.1 million and \$54.6 million of FHLB stock as of March 31, 2011 and December 31, 2010, respectively	99,060	55,932
Total investments	\$ 3,032,940	\$ 3,369,332

Mortgage-backed securities at the indicated dates consist of:

<i>(In thousands)</i>	As of March 31, 2011	As of December 31, 2010
Held-to-maturity		
FHLMC certificates	\$	\$ 2,569
FNMA certificates		416,382
		418,951
Available-for-sale		
FHLMC certificates	3,709	1,817
GNMA certificates	961,337	991,378

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FNMA certificates	251,594	215,059
Collateralized Mortgage Obligations issued or guaranteed by FHLMC, FNMA and GNMA	108,490	114,915
Other mortgage pass-through certificates	68,355	72,317
	1,393,485	1,395,486
Total mortgage-backed securities	\$ 1,393,485	\$ 1,814,437

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The carrying values of investment securities classified as available-for-sale as of March 31, 2011 by contractual maturity (excluding mortgage-backed securities and equity securities) are shown below:

(Dollars in thousands)	Carrying Amount	Weighted Average Yield %
U.S. Government and agencies obligations		
Due within one year	\$ 58,759	0.91
Due after one year through five years	1,108,727	1.23
	1,167,486	1.21
 Puerto Rico Government obligations		
Due within one year	725	6.68
Due after one year through five years	39,963	5.08
Due after five years through ten years	111,648	5.21
Due after ten years	9,518	5.87
	161,854	5.22
 Corporate bonds		
Due after ten years	1,295	5.80
	1,295	5.80
 Total	1,330,635	1.71
 Mortgage-backed securities	1,393,485	3.97
 Equity securities	47	
 Total investment securities available for sale	\$ 2,724,167	2.86

Net interest income of future periods will be affected by the Corporation's decision to deleverage its investment securities portfolio to preserve its capital position and from balance sheet repositioning strategies. Also, net interest income could be affected by prepayments of mortgage-backed securities. Acceleration in the prepayments of mortgage-backed securities would lower yields on these securities, as the amortization of premiums paid upon acquisition of these securities would accelerate. Conversely, acceleration in the prepayments of mortgage-backed securities would increase yields on securities purchased at a discount, as the amortization of the discount would accelerate. These risks are directly linked to future period market interest rate fluctuations. Also, net interest income in future periods might be affected by the Corporation's investment in callable securities. Approximately \$50 million of investment securities, U.S. Agency debentures, with an average yield of 2.00% were called during the first quarter of 2011. As of March 31, 2011, the Corporation has approximately \$366.4 million in debt securities (U.S. agency and Puerto Rico government securities) with embedded calls and with an average yield of 2.34%. Refer to the Risk Management section below for further analysis of the effects of changing interest rates on the Corporation's net interest

income and of the interest rate risk management strategies followed by the Corporation. Also refer to Note 4 to the accompanying unaudited consolidated financial statements for additional information regarding the Corporation's investment portfolio.

RISK MANAGEMENT

Risks are inherent in virtually all aspects of the Corporation's business activities and operations. Consequently, effective risk management is fundamental to the success of the Corporation. The primary goals of risk management are to ensure that the Corporation's risk taking activities are consistent with the Corporation's objectives and risk tolerance and that there is an appropriate balance between risk and reward in order to maximize stockholder value.

The Corporation has in place a risk management framework to monitor, evaluate and manage the principal risks assumed in conducting its activities. First BanCorp's business is subject to eight broad categories of risks: (1) liquidity risk, (2) interest rate risk, (3) market risk, (4) credit risk, (5) operational risk, (6) legal and compliance risk, (7) reputational risk, and (8) contingency risk. First BanCorp has adopted policies and procedures designed to identify and manage risks to which the Corporation is exposed, specifically those relating to liquidity risk, interest rate risk, credit risk, and operational risk.

The Corporation's risk management policies are described below as well as in the Management's Discussion and Analysis of Financial Condition and Results of Operations section of First BanCorp's 2010 Annual Report on Form 10-K.

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Liquidity is the ongoing ability to accommodate liability maturities and deposit withdrawals, fund asset growth and business operations, and meet contractual obligations through unconstrained access to funding at reasonable market rates. Liquidity management involves forecasting funding requirements and maintaining sufficient capacity to meet the needs for liquidity and accommodate fluctuations in asset and liability levels due to changes in the Corporation's business operations or unanticipated events.

The Corporation manages liquidity at two levels. The first is the liquidity of the parent company, which is the holding company that owns the banking and non-banking subsidiaries. The second is the liquidity of the banking subsidiary. As of March 31, 2011, FirstBank could not pay any dividend to the parent company except upon receipt of prior approval by the FED.

The Asset and Liability Committee of the Board of Directors is responsible for establishing the Corporation's liquidity policy as well as approving operating and contingency procedures, and monitoring liquidity on an ongoing basis. The MIALCO, using measures of liquidity developed by management, which involve the use of several assumptions, reviews the Corporation's liquidity position on a monthly basis. The MIALCO oversees liquidity management, interest rate risk and other related matters. The MIALCO, which reports to the Board of Directors' Asset and Liability Committee, is composed of senior management officers, including the Chief Executive Officer, the Chief Financial Officer, the Chief Risk Officer, the Retail Financial Services Director, the Risk Manager of the Treasury and Investments Division, the Asset/Liability Manager, and the Treasurer. The Treasury and Investments Division is responsible for planning and executing the Corporation's funding activities and strategy; monitoring liquidity availability on a daily basis and reviewing liquidity measures on a weekly basis. The Treasury and Investments Accounting and Operations area of the Comptroller's Department is responsible for calculating the liquidity measurements used by the Treasury and Investment Division to review the Corporation's daily and weekly liquidity position and on a monthly basis, the Asset/Liability Manager estimates the liquidity gap for longer periods.

In order to ensure adequate liquidity through the full range of potential operating environments and market conditions, the Corporation conducts its liquidity management and business activities in a manner that will preserve and enhance funding stability, flexibility and diversity. Key components of this operating strategy include a strong focus on the continued development of customer-based funding, the maintenance of direct relationships with wholesale market funding providers, and the maintenance of the ability to liquidate certain assets when, and if, requirements warrant.

The Corporation develops and maintains contingency funding plans. These plans evaluate the Corporation's liquidity position under various operating circumstances and allow the Corporation to ensure that it will be able to operate through periods of stress when access to normal sources of funds is constrained. The plans project funding requirements during a potential period of stress, specify and quantify sources of liquidity, outline actions and procedures for effectively managing through a difficult period, and define roles and responsibilities. In the Contingency Funding Plan, the Corporation stresses the balance sheet and the liquidity position to critical levels that imply difficulties in getting new funds or even maintaining its current funding position, thereby ensuring the ability to honor its commitments, and establishing liquidity triggers monitored by the MIALCO in order to maintain the ordinary funding of the banking business. Three different scenarios are defined in the Contingency Funding Plan: local market event, credit rating downgrade, and a concentration event. They are reviewed and approved annually by the Board of Directors' Asset and Liability Committee.

The Corporation manages its liquidity in a proactive manner, and maintains a sound liquidity position. Multiple measures are utilized to monitor the Corporation's liquidity position, including basic surplus and time-based reserve measures. The Corporation has maintained basic surplus (cash, short-term assets minus short-term liabilities, and secured lines of credit) well in excess of the self-imposed minimum limit of 5% of total assets. As of March 31, 2011, the estimated basic surplus ratio was approximately 11%, including un-pledged investment securities, FHLB lines of credit, and cash. At the end of the quarter, the Corporation had \$486 million available for additional credit on FHLB lines of credit. Unpledged liquid securities as of March 31, 2011 mainly consisted of fixed-rate MBS and U.S. agency debentures totaling approximately \$332 million. The Corporation does not rely on uncommitted inter-bank lines of credit (federal funds lines) to fund its operations and does not include them in the basic surplus computation. The

Corporation has continued to issue brokered CDs pursuant to approvals received from the FDIC to renew or roll over certain amounts through June 30, 2011.

Sources of Funding

The Corporation utilizes different sources of funding to help ensure that adequate levels of liquidity are available when needed. Diversification of funding sources is of great importance to protect the Corporation's liquidity from market disruptions. The principal sources of short-term funds are deposits, including brokered CDs, securities sold under agreements to repurchase, and lines of credit with the FHLB. The Asset Liability Committee of the Board of Directors reviews credit availability on a regular basis. The Corporation has also securitized and sold mortgage loans as a supplementary source of funding. Issuance of commercial paper have also in the past provided additional funding. Long-term funding has also been obtained through the issuance of notes and, to a lesser extent, long-term brokered CDs. The cost of these different alternatives, among other things, is taken into consideration.

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The Corporation has deleveraged its balance sheet by reducing the amounts of brokered CDs. The reductions in brokered CDs are consistent with the requirements of the Order that preclude the issuance of brokered CDs without FDIC approval and require a plan to reduce the amount of brokered CDs. The reductions in brokered CDs are being partly offset by increases in core deposits. Brokered CDs decreased \$538.1 million to \$5.7 billion as of March 31, 2011 from \$6.3 billion as of December 31, 2010. At the same time, as the Corporation focuses on reducing its reliance on brokered deposits, it is seeking to add core deposits.

The Corporation continues to have the support of creditors, including repurchase agreements counterparties, the FHLB, and other agents such as wholesale funding brokers. While liquidity is an ongoing challenge for all financial institutions, management believes that the Corporation's available borrowing capacity and efforts to grow deposits will be adequate to provide the necessary funding for the 2011 business plans. Nevertheless, management's alternative capital preservation strategies can be implemented should adverse liquidity conditions arise. Refer to Capital discussion below for additional information about capital raising efforts that would impact capital and liquidity levels.

The Corporation's principal sources of funding are:

Brokered CDs A large portion of the Corporation's funding has been retail brokered CDs issued by the Bank subsidiary, FirstBank Puerto Rico. Total brokered CDs decreased from \$6.3 billion at year-end 2010 to \$5.7 billion as of March 31, 2011. Although all the regulatory capital ratios exceeded the established well capitalized levels at March 31, 2011, because of the Order with the FDIC, FirstBank cannot be treated as a well capitalized institution under regulatory guidance and cannot replace maturing brokered CDs without the prior approval of the FDIC. Since the issuance of the Order, the FDIC has granted the Bank temporary waivers to enable it to continue accessing the brokered deposit market through June 30, 2011. Also, the Corporation successfully implemented its core deposit growth strategy that has resulted in an increase of \$177.3 million in core deposits during the first quarter of 2011. The average remaining term to maturity of the retail brokered CDs outstanding as of March 31, 2011 is approximately 1.09 years. Approximately 0.5% of the principal value of these certificates are callable at the Corporation's option.

The use of brokered CDs has been particularly important for the growth of the Corporation. The Corporation encounters intense competition in attracting and retaining regular retail deposits in Puerto Rico. The brokered CDs market is very competitive and liquid, and the Corporation has been able to obtain substantial amounts of funding in short periods of time. This strategy has enhanced the Corporation's liquidity position, since the brokered CDs are insured by the FDIC up to regulatory limits, and can be obtained faster than regular retail deposits. Should the FDIC fail to approve waivers for the renewal of brokered CDs, the Corporation would accelerate the deleveraging through a systematic disposition of assets to meet its liquidity needs. During 2011, the Corporation issued \$313.4 million in brokered CDs to renew maturing brokered CDs having an average coupon of 0.89% (all-in cost of 1.16%).

Management believes it will continue to obtain waivers from the restrictions in the issuance of brokered CDs under the Order to meet its obligations and execute its business plans.

The following table presents a maturity summary of brokered and retail CDs with denominations of \$100,000 or higher as of March 31, 2011:

	Total (In thousands)
Three months or less	\$ 774,034
Over three months to six months	1,059,849
Over six months to one year	2,059,795
Over one year	3,140,880
Total	\$ 7,034,558

Certificates of deposit in denominations of \$100,000 or higher include brokered CDs of \$5.7 billion issued to deposit brokers in the form of large (\$100,000 or more) certificates of deposit that are generally participated out by brokers in shares of less than \$100,000 and are therefore insured by the FDIC. Certificates of deposit with denominations of

\$100,000 or higher also include \$21.7 million of deposits through the Certificate of Deposit Account Registry Service (CDARS). In an effort to meet customer needs and provide its customers with the best products and services available, the Corporation's bank subsidiary, FirstBank Puerto Rico, has joined a program that gives depositors the opportunity to insure their money beyond the standard FDIC coverage. CDARS can offer customers access to FDIC insurance coverage beyond the \$250 thousand per account without limit, by placing deposit in multiple banks through a single bank gateway, when they enter into the CDARS Deposit Placement Agreement, while earning attractive returns on their deposits.

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Retail deposits The Corporation's deposit products also include regular savings accounts, demand deposit accounts, money market accounts and retail CDs. Total deposits, excluding brokered CDs, increased by \$195.5 million to \$6.0 billion from the balance of \$5.8 billion as of December 31, 2010, reflecting increases in core-deposit products such as money market, savings and interest-bearing checking accounts. A significant portion of the increase was related to increases in money market accounts and retail CDs in Florida. Successful marketing campaigns and attractive rates were the main reason for the increase in Florida. Increases were also reflected in Puerto Rico, the Corporation's principal market, with an increase of \$78.6 million (mainly retail deposits and public funds) and in the Virgin Islands with an increase of \$18.7 million. Refer to Note 12 in the accompanying unaudited financial statements for further details.

Refer to the *Net Interest Income* discussion above for information about average balances of interest-bearing deposits, and the average interest rate paid on deposits for the quarters ended March 31, 2011 and 2010.

Securities sold under agreements to repurchase The Corporation's investment portfolio is substantially funded with repurchase agreements. Securities sold under repurchase agreements were \$1.4 billion as of March 31, 2011 and December 31, 2010. One of the Corporation's strategies has been the use of structured repurchase agreements and long-term repurchase agreements to reduce exposure to interest rate risk by lengthening the final maturities of its liabilities while keeping funding costs at reasonable levels. All of the \$1.4 billion of repurchase agreements outstanding as of March 31, 2011 consist of structured repurchase agreements. The access to this type of funding was affected by the liquidity turmoil in the financial markets witnessed in the second half of 2008 and in 2009. Certain counterparties are still not willing to extend the term of maturing repurchase agreements. Nevertheless, in addition to short-term repos, the Corporation has been able to maintain access to credit by using cost-effective sources such as FHLB advances. Refer to Note 14 in the accompanying notes to the unaudited interim consolidated financial statements for further details about repurchase agreements outstanding by counterparty and maturities.

Under the Corporation's repurchase agreements, as is the case with derivative contracts, the Corporation is required to pledge cash or qualifying securities to meet margin requirements. To the extent that the value of securities previously pledged as collateral declines due to changes in interest rates, a liquidity crisis or any other factor, the Corporation will be required to deposit additional cash or securities to meet its margin requirements, thereby adversely affecting its liquidity. Given the quality of the collateral pledged, recently the Corporation has not experienced significant margin calls from counterparties arising from credit-quality-related write-downs in valuations and, as of March 31, 2011, it had only \$0.45 million of cash equivalent instruments deposited in connection with collateralized interest rate swap agreements.

Advances from the FHLB The Corporation's Bank subsidiary is a member of the FHLB system and obtains advances to fund its operations under a collateral agreement with the FHLB that requires the Bank to maintain qualifying mortgages as collateral for advances taken. As of March 31, 2011 and December 31, 2010, the outstanding balance of FHLB advances was \$540.4 million and \$653.4 million, respectively. Approximately \$353.4 million of outstanding advances from the FHLB have maturities of over one year. As part of its precautionary initiatives to safeguard access to credit and obtain low interest rates, the Corporation has been pledging assets with the FHLB while at the same time the FHLB has been revising its credit guidelines and haircuts in the computation of the availability of credit lines.

Though currently not in use, other sources of short-term funding for the Corporation include commercial paper and federal funds purchased. Furthermore, in previous years the Corporation entered into several financing transactions to diversify its funding sources, including the issuance of notes payable and Junior subordinated debentures as part of its longer-term liquidity and capital management activities. No assurance can be given that these sources of liquidity will be available and, if available, will be on comparable terms. The Corporation continues to evaluate its financing options, including available options resulting from federal government initiatives to deal with the crisis in the financial markets.

With respect to the Corporation's \$231.9 million of outstanding subordinated debentures, we have provided, within the time frame prescribed by the indentures governing the subordinated debentures, a notice to the trustees of the subordinated debentures of our election to extend the interest payments on the debentures. Under the indentures, we have the right, from time to time, and without causing an event of default, to defer payments of interest on the subordinated debentures by extending the interest payment period at any time and from time to time during the term of

the subordinated debentures for up to twenty consecutive quarterly periods. We have elected to defer the interest payments that were due in September and December 2010 and in March 2011 because the Federal Reserve advised us that it would not provide its approval for the payment of interest on these subordinated debentures.

The Corporation's principal uses of funds are the origination of loans and the repayment of maturing deposits and borrowings. The Corporation has committed substantial resources to its mortgage banking subsidiary, FirstMortgage Inc. As a result, the ratio of residential real estate loans as a percentage of total loans has increased over time from 14% at December 31, 2004 to 26% at March 31, 2011. Commensurate with the increase in its mortgage banking activities, the Corporation has also invested in technology and personnel to enhance the Corporation's secondary mortgage market capabilities. The enhanced capabilities improve the Corporation's liquidity profile as they allow the Corporation to derive liquidity, if needed, from the sale of mortgage loans in the secondary market. The U.S. (including Puerto Rico) secondary mortgage market is still highly liquid in large part because of the sale or guarantee

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programs of the FHA, VA, HUD, FNMA and FHLMC. The Corporation obtained Commitment Authority to issue GNMA mortgage-backed securities from GNMA and, under this program, the Corporation completed the securitization of approximately \$41.5 million of FHA/VA mortgage loans into GNMA MBS during the first quarter of 2011. Any regulatory actions affecting GNMA, FNMA or FHLMC could adversely affect the secondary mortgage market.

Impact of Credit Ratings on Access to Liquidity and Valuation of Liabilities

The Corporation's credit as a long-term issuer is currently rated CCC+ with negative outlook by Standard & Poor's (S&P) and CC by Fitch Ratings Limited (Fitch). At the FirstBank subsidiary level, long-term issuer ratings are currently Caa2 with negative outlook by Moody's Investor Service (Moody's), eight notches below their definition of investment grade; CCC+ with negative outlook by S&P seven notches below their definition of investment grade, and CC by Fitch, eight notches below their definition of investment grade.

During 2010, the Corporation suffered credit rating downgrades from S&P (from B to CCC+), and Fitch (from B- to CC) rating services. The FirstBank subsidiary also experienced credit rating downgrades in 2010: Moody's from B1 to B3, S&P from B to CCC+, and Fitch from B to CC. Furthermore, in April 2011 Moody's downgraded the Bank's credit rating from B3 to Caa2 with negative outlook. The Corporation does not have any outstanding debt or derivative agreements that would be affected by the recent credit downgrades. Furthermore, given our non-reliance on corporate debt or other instruments directly linked in terms of pricing or volume to credit ratings, the liquidity of the Corporation so far has not been affected in any material way by the downgrades. The Corporation's ability to access new non-deposit sources of funding, however, could be adversely affected by these credit ratings and any additional downgrades.

The Corporation's liquidity is contingent upon its ability to obtain new external sources of funding to finance its operations. The Corporation's current credit ratings and any further downgrades in credit ratings can hinder the Corporation's access to external funding and/or cause external funding to be more expensive, which could in turn adversely affect results of operations. Also, changes in credit ratings may further affect the fair value of certain liabilities and unsecured derivatives that consider the Corporation's own credit risk as part of the valuation.

Cash Flows

Cash and cash equivalents were \$873.3 million and \$1.3 billion at March 31, 2011 and 2010, respectively. These balances increased by \$503.0 million and \$626.1 million from December 31, 2010 and 2009, respectively. The following discussion highlights the major activities and transactions that affected the Corporation's cash flows during the first quarter of 2011 and 2010.

Cash Flows from Operating Activities

First BanCorp's operating assets and liabilities vary significantly in the normal course of business due to the amount and timing of cash flows. Management believes cash flows from operations, available cash balances and the Corporation's ability to generate cash through short- and long-term borrowings will be sufficient to fund the Corporation's operating liquidity needs.

For the first quarter of 2011, net cash provided by operating activities was \$43.6 million. Net cash generated from operating activities was higher than net loss reported largely as a result of adjustments for operating items such as the provision for loan and lease losses, partially offset by adjustments to net income from gain on sale of investments.

For the first quarter of 2010, net cash provided by operating activities was \$83.3 million, which was higher than net income, mainly also as a result of adjustments for operating items such as the provision for loan and lease losses.

Cash Flows from Investing Activities

The Corporation's investing activities primarily include originating loans to be held to maturity and purchasing, selling and repayments of its available-for-sale and held-to-maturity investment securities. For the quarter ended March 31, 2011, net cash provided by investing activities was \$920.8 million, primarily reflecting proceeds from loans, as well as proceeds from securities sold or called during the first quarter of 2011 and MBS prepayments. Proceeds from sales of securities during 2011 and from repayments of loans and MBS were used for loan origination disbursements and paydown of maturing brokered CDs and FHLB Advances.

For the first quarter of 2010, net cash provided by investing activities was \$1.2 billion, primarily from loan repayments and proceeds from securities sold or called.

Table of Contents*Cash Flows from Financing Activities*

The Corporation's financing activities primarily include the receipt of deposits and issuance of brokered CDs, the issuance and payments of long-term debt, the issuance of equity instruments and activities related to its short-term funding. In addition, the Corporation paid monthly dividends on its preferred stock and quarterly dividends on its common stock until it announced the suspension of dividends beginning in August 2009. In the first quarter of 2011, net cash used in financing activities was \$461.5 million due to paydowns of maturing brokered CDs coupled with paydowns of FHLB Advances.

In the first quarter of 2010, net cash used in financing activities was \$691.3 million due to paydowns of FHLB and FED advances and maturing repurchase agreements, partially offset by growth in the core deposit base.

Capital

The Corporation's stockholders' equity amounted to \$1.0 billion as of March 31, 2011, a decrease of \$30.7 million compared to the balance as of December 31, 2010, driven by the net loss of \$28.4 million for the first quarter and a decrease of \$2.3 million in other comprehensive income due to lower unrealized gains on available for sale securities. Based on the Agreement with the FED, currently neither First BanCorp, nor FirstBank, is permitted to pay dividends on capital securities without prior approval.

Effective June 2, 2010, FirstBank, by and through its Board of Directors, entered into the Order with the FDIC (see Description of Business). Although all the regulatory capital ratios exceeded the established "well capitalized" levels at March 31, 2011, because of the Order with the FDIC, FirstBank cannot be treated as a "well capitalized" institution under regulatory guidance. Set forth below are First BanCorp's, and FirstBank Puerto Rico's regulatory capital ratios as of March 31, 2011 and December 31, 2010, based on existing established FED and FDIC guidelines.

	First		Banking Subsidiary	
	BanCorp	FirstBank	To be well	Consent Order
			capitalized	Requirements over
				time
As of March 31, 2011				
Total capital (Total capital to risk-weighted assets)	11.97%	11.71%	10.00%	12.00%
Tier 1 capital ratio (Tier 1 capital to risk-weighted assets)	10.65%	10.40%	6.00%	10.00%
Leverage ratio	7.78%	7.60%	5.00%	8.00%
As of December 31, 2010				
Total capital (Total capital to risk-weighted assets)	12.02%	11.57%	10.00%	12.00%
Tier 1 capital ratio (Tier 1 capital to risk-weighted assets)	10.73%	10.28%	6.00%	10.00%
Leverage ratio	7.57%	7.25%	5.00%	8.00%

The improvement in the capital ratios for FirstBank was primarily related to a \$22 million capital contribution from the holding company and due to the significant decrease in risk-weight and total average assets consistent with the Corporation's actions to deleverage and de-risk the balance sheet.

The Consent Order required that FirstBank submit a Capital Plan to the FDIC detailing the manner by which it would achieve a total capital to risk-weighted assets ratio of at least 12%, a Tier 1 capital to risk-weighted assets ratio of at least 10% and a leverage ratio of at least 8% over time. In this respect, FirstBank submitted in March 2011, an updated Capital Plan that contemplates a \$350 million capital raise through the issuance of new common shares for cash, and other actions to further reduce the Corporation's and FirstBank's risk-weighted assets, strengthened their capital positions and meet the minimum capital ratios required for FirstBank under the Consent Order. The Capital

Plan identifies specific targeted leverage, Tier 1 risk-based capital and total risk-based capital ratios to be achieved each calendar quarter until the capital levels required under the Order are achieved. As of March 31, 2011, all capital ratios for FirstBank are above the Capital Plan's targeted levels and the Corporation expects to be in compliance with the minimum capital ratios under the FDIC Order by June 30, 2011.

If the Bank fails to achieve the capital ratios as provided in the FDIC Order, within 45 days of being out of compliance, the Bank would be required to increase capital in an amount sufficient to comply with the capital ratios set forth in the Capital Plan, or submit to the regulators a contingency plan for the sale, merger, or liquidation of the institution in the event the primary sources of capital are not available. Thereafter the FDIC would determine whether and when to initiate an acceptable contingency plan.

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Should the Corporation's efforts to raise capital not be completed, the Corporation's Capital Plan includes other actions which could allow the Bank to attain the minimum capital ratios under the FDIC Order. The strategies incorporated into the Capital Plan to meet the minimum capital ratios include the following:

Strategies completed during the first quarter of 2011:

Sale of performing first lien residential mortgage loans The Bank sold approximately \$236 million in mortgage loans to another financial institution during February 2011. Proceeds were used, in part, to reduce funding sources and to support liquidity reserves.

Sale of Investment securities The Bank sold approximately \$330 million in investment securities during March 2011. Proceeds were used, in part, to reduce funding sources and to support liquidity reserves.

The Corporation contributed \$22 million of capital to the Bank during March 2011.

Strategies completed or expected to be completed by June 30, 2011:

Sale of performing first lien residential mortgage loans- The Bank entered into a letter of intent to sell mortgage loans before June 30, 2011. During the first quarter of 2011, the Corporation reclassified from held to investment to held for sale approximately \$282 million related to this transaction. The loans were sold in April 2011.

Sale of investment securities The Bank sold approximately \$268 million in investment securities on April 6, 2011.

Sale of commercial loan participations The Bank has commenced negotiations to sell approximately \$150 million in loan participations to other financial institutions by June 30, 2011.

The proceeds received from the above three transactions will be used to reduce funding sources.

Upon the successful completion of these actions, when combined with the achievement of operating results in line with management's current expectations, management expects that the Corporation and the Bank will attain the minimum capital ratios set forth in the Capital Plan. However, no assurance can be given that the Corporation and the Bank will be able to achieve such ratios.

In the event the Corporation is unable to complete its capital raising efforts during 2011 and actual credit losses exceed amounts projected, the Capital Plan includes additional actions designed to allow the Bank to maintain the minimum capital ratios for the foreseeable future, including the sale of additional assets. The Corporation's tangible common equity ratio decreased to 3.71% as of March 31, 2011, from 3.80% as of December 31, 2010, and the Tier 1 common equity to risk-weighted assets ratio as of March 31, 2011 decreased to 4.82% from 5.01% as of December 31, 2010.

The tangible common equity ratio and tangible book value per common share are non-GAAP measures generally used by the financial community to evaluate capital adequacy. Tangible common equity is total equity less preferred equity, goodwill and core deposit intangibles. Tangible assets are total assets less goodwill and core deposit intangibles. Management and many stock analysts use the tangible common equity ratio and tangible book value per common share in conjunction with more traditional bank capital ratios to compare the capital adequacy of banking organizations with significant amounts of goodwill or other intangible assets, typically stemming from the use of the purchase accounting method of accounting for mergers and acquisitions. Neither tangible common equity, nor tangible assets, or related measures should be considered in isolation or as a substitute for stockholders' equity, total assets or any other measure calculated in accordance with GAAP. Moreover, the manner in which the Corporation calculates its tangible common equity, tangible assets and any other related measures may differ from that of other companies reporting measures with similar names.

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The following table is a reconciliation of the Corporation's tangible common equity and tangible assets for the periods ended March 31, 2011 and December 31, 2010, respectively:

<i>(In thousands)</i>	March 31, 2011	December 31, 2010
Total equity - GAAP	\$ 1,027,269	\$ 1,057,959
Preferred equity	(426,724)	(425,009)
Goodwill	(28,098)	(28,098)
Core deposit intangible	(13,454)	(14,043)
Tangible common equity	\$ 558,993	\$ 590,809
Total assets - GAAP	\$ 15,104,090	\$ 15,593,077
Goodwill	(28,098)	(28,098)
Core deposit intangible	(13,454)	(14,043)
Tangible assets	\$ 15,062,538	\$ 15,550,936
Common shares outstanding	21,304	21,304
Tangible common equity ratio	3.71%	3.80%
Tangible book value per common share	\$ 26.24	\$ 27.73

The Tier 1 common equity to risk-weighted assets ratio is calculated by dividing (a) tier 1 capital less non-common elements including qualifying perpetual preferred stock and qualifying trust preferred securities by (b) risk-weighted assets, which assets are calculated in accordance with applicable bank regulatory requirements. The Tier 1 common equity ratio is not required by GAAP or on a recurring basis by applicable bank regulatory requirements. However, this ratio was used by the Federal Reserve in connection with its stress test administered to the 19 largest U.S. bank holding companies under the Supervisory Capital Assessment Program (SCAP), the results of which were announced on May 7, 2009. Management is currently monitoring this ratio, along with the other ratios discussed above, in evaluating the Corporation's capital levels and believes that, at this time, the ratio may be of interest to investors.

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The following table reconciles stockholders' equity (GAAP) to Tier 1 common equity:

<i>(In thousands)</i>	March 31, 2011	December 31, 2010
Total equity - GAAP	\$ 1,027,269	\$ 1,057,959
Qualifying preferred stock	(426,724)	(425,009)
Unrealized gain on available-for-sale securities (1)	(15,453)	(17,736)
Disallowed deferred tax asset (2)	(981)	(815)
Goodwill	(28,098)	(28,098)
Core deposit intangible	(13,454)	(14,043)
Cumulative change gain in fair value of liabilities accounted for under a fair value option	(2,156)	(2,185)
Other disallowed assets	(881)	(226)
Tier 1 common equity	\$ 539,522	\$ 569,847
Total risk-weighted assets	\$ 11,183,518	\$ 11,372,856
Tier 1 common equity to risk-weighted assets ratio	4.82%	5.01%

- 1- Tier 1 capital excludes net unrealized gains (losses) on available-for-sale debt securities and net unrealized gains on available-for-sale equity securities with readily determinable fair values, in accordance with regulatory risk-based capital guidelines. In arriving at Tier 1 capital, institutions are required to deduct net unrealized losses on available-for-sale equity securities with readily determinable fair values, net of tax.
- 2- Approximately \$12 million and \$13 million of the Corporation's net deferred tax assets at March 31, 2011 and December 31, 2010, respectively were included without limitation in regulatory capital pursuant to the risk-based capital guidelines, while approximately \$1.0 million of such assets at March 31, 2011 and \$0.8 million at December 31, 2010 exceeded the limitation imposed by these guidelines and, as disallowed deferred tax assets, were deducted in arriving at Tier 1 capital. According to regulatory capital guidelines, the deferred tax assets that are dependent upon future taxable income are limited for inclusion in Tier 1 capital to the lesser of: (i) the amount of such deferred tax asset that the entity expects to realize within one year of the calendar quarter end-date, based on its projected future taxable income for that year or (ii) 10% of the amount of the entity's Tier 1 capital. Approximately \$5 million of the Corporation's other net deferred tax liability at March 31, 2011 and December 31, 2010 represented primarily the deferred tax effects of unrealized gains and losses on available-for-sale debt securities, which are permitted to be excluded prior to deriving the amount of net deferred tax assets subject to limitation under the guidelines.

Off-Balance Sheet Arrangements

In the ordinary course of business, the Corporation engages in financial transactions that are not recorded on the balance sheet, or may be recorded on the balance sheet in amounts that are different than the full contract or notional amount of the transaction. These transactions are designed to (1) meet the financial needs of customers, (2) manage the Corporation's credit, market or liquidity risks, (3) diversify the Corporation's funding sources and (4) optimize capital.

As a provider of financial services, the Corporation routinely enters into commitments with off-balance sheet risk to meet the financial needs of its customers. These financial instruments may include loan commitments and standby letters of credit. These commitments are subject to the same credit policies and approval process used for on-balance sheet instruments. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of

the amount recognized in the statement of financial position. As of March 31, 2011, commitments to extend credit and commercial and financial standby letters of credit amounted to approximately \$667.9 million and \$80.5 million, respectively. Commitments to extend credit are agreements to lend to customers as long as the conditions established in the contract are met. Generally, the Corporation's mortgage banking activities do not enter into interest rate lock agreements with its prospective borrowers.

Table of Contents**Contractual Obligations and Commitments**

The following table presents a detail of the maturities of the Corporation's contractual obligations and commitments, which consist of CDs, long-term contractual debt obligations, commitments to sell mortgage loans and commitments to extend credit:

	Contractual Obligations and Commitments				
	As of March 31, 2011				
	Total	Less than 1 year	1-3 years	3-5 years	After 5 years
	(In thousands)				
Contractual obligations:					
Certificates of deposit	7,984,500	4,538,028	3,360,144	72,249	14,079
Securities sold under agreements to repurchase	1,400,000	100,000	700,000	600,000	
Advances from FHLB	540,440	187,000	353,440		
Notes payable	27,837	15,400			12,437
Other borrowings	231,959				231,959
Total contractual obligations	\$ 10,184,736	\$ 4,840,428	\$ 4,413,584	\$ 672,249	\$ 258,475
 Commitments to sell mortgage loans	 \$ 27,571	 \$ 27,571			
Standby letters of credit	\$ 30,133	\$ 30,133			
 Commitments to extend credit:					
Lines of credit	\$ 509,861	\$ 509,861			
Letters of credit	50,389	50,389			
Commitments to originate loans	158,008	108,008	50,000		
Total commercial commitments	\$ 718,258	\$ 668,258	\$ 50,000		

The Corporation has obligations and commitments to make future payments under contracts, such as debt and lease agreements, and under other commitments to sell mortgage loans at fair value and to extend credit. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Other contractual obligations result mainly from contracts for the rental and maintenance of equipment. Since certain commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. For most of the commercial lines of credit, the Corporation has the option to reevaluate the agreement prior to additional disbursements. There have been no significant or unexpected draws on existing commitments. In the case of credit cards and personal lines of credit, the Corporation can at any time and without cause cancel the unused credit facility. In the ordinary course of business, the Corporation enters into operating leases and other commercial commitments. There have been no significant changes in such contractual obligations since December 31, 2010.

Lehman Brothers Special Financing, Inc. (Lehman) was the counterparty to the Corporation on certain interest rate swap agreements. During the third quarter of 2008, Lehman failed to pay the scheduled net cash settlement due to the Corporation, which constituted an event of default under those interest rate swap agreements. The Corporation terminated all interest rate swaps with Lehman and replaced them with other counterparties under similar terms and conditions. In connection with the unpaid net cash settlement due as of March 31, 2011 under the swap agreements, the Corporation has an unsecured counterparty exposure with Lehman, which filed for bankruptcy on October 3, 2008,

of approximately \$1.4 million. This exposure was reserved in the third quarter of 2008. The Corporation had pledged collateral of \$63.6 million with Lehman to guarantee its performance under the swap agreements in the event payment there under was required. The book value of pledged securities with Lehman as of December 31, 2010 amounted to approximately \$64.5 million.

The Corporation believes that the securities pledged as collateral should not be part of the Lehman bankruptcy estate given the fact that the posted collateral constituted a performance guarantee under the swap agreements and was not part of a financing agreement, and that ownership of the securities was never transferred to Lehman. Upon termination of the interest rate swap agreements, Lehman's obligation was to return the collateral to the Corporation. During the fourth quarter of 2009, the Corporation discovered that Lehman Brothers, Inc., acting as agent of Lehman, had deposited the securities in a custodial account at JP Morgan Chase, and that, shortly before the filing of the Lehman bankruptcy proceedings, it had provided instructions to have most of the securities transferred to Barclays Capital (Barclays) in New York. After Barclays's refusal to turn over the securities, during December 2009, the Corporation filed a lawsuit against Barclays in federal court in New York demanding the return of the securities.

During February 2010, Barclays filed a motion with the court requesting that the Corporation's claim be dismissed on the grounds that the allegations of the complaint are not sufficient to justify the granting of the remedies therein sought. Shortly thereafter, the Corporation filed its opposition motion. A hearing on the motions was held in court on April 28, 2010. The court, on that date, after hearing the arguments by both sides, concluded that the Corporation's equitable-based causes of action, upon which the return of the investment securities is being demanded, contain allegations that sufficiently plead facts warranting the denial of Barclays' motion to dismiss the Corporation's claim. Accordingly, the judge ordered the case to proceed to trial. Subsequent to the court decision, the district court judge transferred the case to the Lehman bankruptcy court for trial. While the Corporation believes it has valid reasons to support its claim for the

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return of the securities, the Corporation may not succeed in its litigation against Barclays to recover all or a substantial portion of the securities. Upon such transfer, the Bankruptcy court began to entertain the pre-trial procedures including discovery of evidence. In this regard, an initial scheduling conference was held before the United States Bankruptcy Court for the Southern District of New York on November 17, 2010, at which time a proposed case management plan was approved. Discovery has commenced pursuant to that case management plan and is currently scheduled for completion by September 15, 2011, but this timing is subject to adjustment.

Additionally, the Corporation continues to pursue its claim filed in January 2009 in the proceedings under the Securities Protection Act with regard to Lehman Brothers Incorporated in Bankruptcy Court, Southern District of New York. An estimated loss was not accrued as the Corporation is unable to determine the timing of the claim resolution or whether it will succeed in recovering all or a substantial portion of the collateral or its equivalent value. If additional relevant negative facts become available in future periods, a need to recognize a partial or full reserve of this claim may arise. Considering that the investment securities have not yet been recovered by the Corporation, despite its efforts in this regard, the Corporation decided to classify such investments as non-performing during the second quarter of 2009.

Interest Rate Risk Management

First BanCorp manages its asset/liability position in order to limit the effects of changes in interest rates on net interest income and to maintain stability of profitability under varying interest rate scenarios. The MIALCO oversees interest rate risk and meetings focus on, among other things, current and expected conditions in world financial markets, competition and prevailing rates in the local deposit market, liquidity, securities market values, recent or proposed changes to the investment portfolio, alternative funding sources and related costs, hedging and the possible purchase of derivatives such as swaps and caps, and any tax or regulatory issues which may be pertinent to these areas. The MIALCO approves funding decisions in light of the Corporation's overall strategies and objectives.

The Corporation performs on a quarterly basis a consolidated net interest income simulation analysis to estimate the potential change in future earnings from projected changes in interest rates. These simulations are carried out over a one-to-five-year time horizon, assuming upward and downward yield curve shifts. The rate scenarios considered in these disclosures reflect gradual upward and downward interest rate movements of 200 basis points, during a twelve-month period. Simulations are carried out in two ways:

- (1) Using a static balance sheet, as the Corporation had it on the simulation date, and
- (2) Using a dynamic balance sheet based on recent patterns and current strategies.

The balance sheet is divided into groups of assets and liabilities detailed by maturity or re-pricing structure and their corresponding interest yields and costs. As interest rates rise or fall, these simulations incorporate expected future lending rates, current and expected future funding sources and costs, the possible exercise of options, changes in prepayment rates, deposits decay and other factors which may be important in projecting net interest income.

The Corporation uses a simulation model to project future movements in the Corporation's balance sheet and income statement. The starting point of the projections generally corresponds to the actual values on the balance sheet on the date of the simulations.

These simulations are highly complex, and are based on many assumptions that are intended to reflect the general behavior of the balance sheet components over the period in question. It is unlikely that actual events will match these assumptions in all cases. For this reason, the results of these forward-looking computations are only approximations of the true sensitivity of net interest income to changes in market interest rates.

The following table presents the results of the simulations as of March 31, 2011 and December 31, 2010. Consistent with prior years, these exclude non-cash changes in the fair value of derivatives and liabilities elected to be measured at fair value:

March 31, 2011		December 31, 2010	
Net Interest Income Risk (Projected for the next 12 months)		Net Interest Income Risk (Projected for the next 12 months)	
Static Simulation	Growing Balance Sheet	Static Simulation	Growing Balance Sheet

(Dollars in millions)	\$ Change	% Change	\$ Change	% Change	\$ Change	% Change	\$ Change	% Change
+ 200 bps ramp	\$ 20.7	4.96%	\$ 19.6	4.85%	\$ 24.8	5.37%	\$ 24.8	5.60%
- 200 bps ramp	\$(11.7)	(2.81)%	\$(15.4)	(3.83)%	\$(22.8)	(4.94)%	\$(24.2)	(5.48)%

The Corporation continues to manage its balance sheet structure to control the overall interest rate risk and preserve its capital position. The Corporation continued with a deleveraging and balance sheet repositioning strategy. During the first quarter of 2011, the investment portfolio decreased by approximately \$430 million, while the loan portfolio decreased by \$570 million. This decrease in assets resulting from the deleveraging strategy allowed a reduction of approximately \$651 million in wholesale funding since the end of the fourth quarter of 2010, including FHLB Advances and Brokered CDs. In addition, the Corporation continues to grow its core deposit base while adjusting the mix of its funding sources to better match the expected average life of the assets.

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Taking into consideration the above-mentioned facts for modeling purposes, the net interest income for the next twelve months under a non-static balance sheet scenario, is estimated to increase by \$19.6 million in a gradual parallel upward move of 200 basis points.

Following the Corporation's risk management policies, modeling of the downward parallel rates moves by anchoring the short end of the curve, (falling rates with a flattening curve) was performed, even though, given the current level of rates as of March 31, 2011, some market interest rate were projected to be zero. Under this scenario the net interest income for the next twelve months in a non-static balance sheet scenario is estimated to decrease by \$15.4 million.

Derivatives

First BanCorp uses derivative instruments and other strategies to manage its exposure to interest rate risk caused by changes in interest rates beyond management's control.

The following summarizes major strategies, including derivative activities, used by the Corporation in managing interest rate risk:

Interest rate cap agreements Interest rate cap agreements provide the right to receive cash if a reference interest rate rises above a contractual rate. The value increases as the reference interest rate rises. The Corporation enters into interest rate cap agreements for protection from rising interest rates. Specifically, the interest rate on certain of the Corporation's commercial loans to other financial institutions is generally a variable rate limited to the weighted-average coupon of the referenced residential mortgage collateral, less a contractual servicing fee. During the second quarter of 2010, the counterparty for interest rate caps for certain private label MBS was taken over by the FDIC, which resulted in the immediate cancelation of all outstanding commitments, and as a result, interest rate caps with a notional amount of \$103 million are no longer considered to be derivative financial instruments. The total exposure to fair value of \$3.0 million related to such contracts was reclassified to an account receivable.

Interest rate swaps Interest rate swap agreements generally involve the exchange of fixed and floating-rate interest payment obligations without the exchange of the underlying notional principal amount. As of March 31, 2011, most of the interest rate swaps outstanding are used for protection against rising interest rates. Similar to unrealized gains and losses arising from changes in fair value, net interest settlements on interest rate swaps are recorded as an adjustment to interest income or interest expense depending on whether an asset or liability is being economically hedged.

Indexed options Indexed options are generally over-the-counter (OTC) contracts that the Corporation enters into in order to receive the appreciation of a specified Stock Index (e.g., Dow Jones Industrial Composite Stock Index) over a specified period in exchange for a premium paid at the contract's inception. The option period is determined by the contractual maturity of the notes payable tied to the performance of the Stock Index. The credit risk inherent in these options is the risk that the exchange party may not fulfill its obligation.

Forward Contracts Forward contracts are sales of to-be-announced (TBA) mortgage-backed securities that will settle over the standard delivery date and do not qualify as regular way security trades. Regular-way security trades are contracts with no net settlement provision and no market mechanism to facilitate net settlement and they provide for delivery of a security within the time generally established by regulations or conventions in the market-place or exchange in which the transaction is being executed. The forward sales are considered derivative instruments that need to be marked-to-market. These securities are used to hedge the loan production of GNMA securities of the mortgage-banking operations. Unrealized gains (losses) are recognized as part of mortgage banking activities in the Consolidated Statement of (Loss) Income.

For detailed information regarding the volume of derivative activities (e.g. notional amounts), location and fair values of derivative instruments in the Statement of Financial Condition and the amount of gains and losses reported in the Statement of Loss, refer to Note 9 in the accompanying unaudited consolidated financial statements.

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The following tables summarize the fair value changes in the Corporation's derivatives as well as the sources of the fair values:

(In thousands)	Three-month period ended March 31, 2011
Fair value of contracts outstanding at the beginning of the period	\$ (4,796)
Changes in fair value during the period	76
Fair value of contracts outstanding as of March 31, 2010	\$ (4,720)

Source of Fair Value

(In thousands)	Payments Due by Period					Total Fair Value
	Maturity Less Than One Year	Maturity 1-3 Years	Maturity 3-5 Years	In Excess of 5 Years	Maturity	
As of March 31, 2011						
Pricing from observable market inputs	\$ (224)	\$ (585)	\$ 15	\$ (3,926)		\$ (4,720)
	\$ (224)	\$ (585)	\$ 15	\$ (3,926)		\$ (4,720)

Derivative instruments, such as interest rate swaps, are subject to market risk. As is the case with investment securities, the market value of derivative instruments 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 as well as the level of interest rates.

As of March 31, 2011 and December 31, 2010, all of the derivative instruments held by the Corporation were considered economic undesignated hedges.

The use of derivatives involves market and credit risk. The market risk of derivatives stems principally from the potential for changes in the value of derivative contracts based on changes in interest rates. The credit risk of derivatives arises from the potential of default from the counterparty. To manage this credit risk, the Corporation deals with counterparties of good credit standing, enters into master netting agreements whenever possible and, when appropriate, obtains collateral. Master netting agreements incorporate rights of set-off that provide for the net settlement of contracts with the same counterparty in the event of default. Currently the Corporation is mostly engaged in derivative instruments with counterparties with a credit rating of single A or better. All of the Corporation's interest rate swaps are supported by securities collateral agreements, which allow the delivery of securities to and from the counterparties depending on the fair value of the instruments, to minimize credit risk.

Refer to Note 20 of the accompanying unaudited consolidated financial statements for additional information regarding the fair value determination of derivative instruments.

Set forth below is a detailed analysis of the Corporation's credit exposure by counterparty with respect to derivative instruments outstanding as of March 31, 2011 and December 31, 2010.

(In thousands)	As of March 31, 2011			Accrued interest receivable
	Total Exposure at	Negative	Total	

Counterparty	Rating⁽¹⁾	Notional	Fair Value⁽²⁾	Fair Values	Fair Value	(payable)
Interest rate swaps with rated counterparties:						
JP Morgan	A+	\$ 42,420	\$ 1,291	\$ (4,512)	\$ (3,221)	\$
Credit Suisse First Boston	A+	5,484		(301)	(301)	
Goldman Sachs	A	6,515	916		916	
Morgan Stanley	A	108,600	1		1	
		163,019	2,208	(4,813)	(2,605)	
Other derivatives:						
Other derivatives (3)		154,599	348	(2,463)	(2,115)	(139)
Total		\$ 317,618	\$ 2,556	\$ (7,276)	\$ (4,720)	\$ (139)

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As of December 31, 2010						
(In thousands)			Total Exposure at Fair Value ⁽²⁾	Negative Fair Values	Total Fair Value	Accrued interest receivable (payable)
Counterparty	Rating ⁽¹⁾	Notional				
Interest rate swaps with rated counterparties:						
JP Morgan	A+	\$ 42,808	\$ 889	\$ (4,865)	\$ (3,976)	\$
Credit Suisse First Boston	A+	5,493		(327)	(327)	
Goldman Sachs	A	6,515	664		664	
Morgan Stanley	A	108,829	1		1	
		163,645	1,554	(5,192)	(3,638)	
Other derivatives:						
Other derivatives (3)		127,837	351	(1,509)	(1,158)	(140)
Total		\$ 291,482	\$ 1,905	\$ (6,701)	\$ (4,796)	\$ (140)

(1) Based on the S&P and Fitch Long Term Issuer Credit Ratings.

(2) For each counterparty, this amount includes derivatives with positive fair value excluding the related accrued interest receivable/payable.

(3) Credit exposure with several Puerto Rico counterparties for which a credit rating is not readily available.

A Hull-White Interest Rate Tree approach is used to value the option components of derivative instruments. The discounting of the cash flows is performed using US dollar LIBOR-based discount rates or yield curves that account for the industry sector and the credit rating of the counterparty and/or the Corporation. Although most of the derivative instruments are fully collateralized, a credit spread is considered for those that are not secured in full. The cumulative mark-to-market effect of credit risk in the valuation of derivative instruments resulted in an unrealized gain of approximately \$0.6 million as of March 31, 2011, which includes an unrealized loss of \$0.2 million recorded in the first quarter of 2011 and an unrealized loss of \$0.1 million for the first quarter of 2010. The Corporation compares the valuations obtained with valuations received from counterparties, as an internal control procedure.

Credit Risk Management

First BanCorp is subject to credit risk mainly with respect to its portfolio of loans receivable and off-balance sheet instruments, mainly derivatives and loan commitments. Loans receivable represents loans that First BanCorp holds for investment and, therefore, First BanCorp is at risk for the term of the loan. Loan commitments represent commitments to extend credit, subject to specific condition, for specific amounts and maturities. These commitments may expose the Corporation to credit risk and are subject to the same review and approval process as for loans. Refer to

Contractual Obligations and Commitments above for further details. The credit risk of derivatives arises from the potential of the counterparty's default on its contractual obligations. To manage this credit risk, the Corporation deals with counterparties of good credit standing, enters into master netting agreements whenever possible and, when appropriate, obtains collateral. For further details and information on the Corporation's derivative credit risk exposure, refer to Interest Rate Risk Management section above. The Corporation manages its credit risk through credit policy, underwriting, independent loan review and quality control procedures, statistical analysis, comprehensive financial analysis, and established management committees. The Corporation also employs proactive collection and loss

mitigation efforts. Furthermore, personnel performing structured loan workout functions are responsible for avoiding defaults and minimizing losses upon default within each region and for each business segment. In the case of commercial and industrial, commercial mortgage and construction loan portfolios, the Special Asset Group (SAG) focuses on strategies for the accelerated reduction of non-performing assets through note sales, loss mitigation programs, and sales of REO. In addition to the management of the resolution process for problem loans, the SAG oversees collection efforts for all loans to prevent migration to the non-performing and/or adversely classified status. The SAG utilizes relationship officers, collection specialists and attorneys. In the case of residential construction projects, the workout function monitors project specifics, such as project management and marketing, as deemed necessary.

The Corporation may also have risk of default in the securities portfolio. The securities held by the Corporation are principally fixed-rate mortgage-backed securities and U.S. Treasury and agency securities. Thus, a substantial portion of these instruments is backed by mortgages, a guarantee of a U.S. government-sponsored entity or backed by the full faith and credit of the U.S. government and is deemed to be of the highest credit quality.

Management, comprised of the Corporation's Commercial Credit Risk Officer, Retail Credit Risk Officer, Chief Lending Officer and other senior executives, has the primary responsibility for setting strategies to achieve the Corporation's credit risk goals and objectives. Those goals and objectives are documented in the Corporation's Credit Policy.

Allowance for Loan and Lease Losses and Non-performing Assets

Allowance for Loan and Lease Losses

The allowance for loan and lease losses represents the estimate of the level of reserves appropriate to absorb inherent credit losses. The amount of the allowance was determined by empirical analysis and judgments regarding the quality of each individual loan portfolio. All known relevant internal and external factors that affected loan collectibility were considered, including analyses of

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historical charge-off experience, migration patterns, changes in economic conditions, and changes in loan collateral values. For example, factors affecting the economies of Puerto Rico, Florida (USA), the US Virgin Islands and the British Virgin Islands may contribute to delinquencies and defaults above the Corporation's historical loan and lease losses. Such factors are subject to regular review and may change to reflect updated performance trends and expectations, particularly in times of severe stress such as have been experienced since 2008. The process includes judgmental and quantitative elements that may be subject to significant change. There is no certainty that the allowance will be adequate over time to cover credit losses in the portfolio because of continued adverse changes in the economy, market conditions, or events adversely affecting specific customers, industries or markets. To the extent actual outcomes differ from our estimates, the credit quality of our customer base materially decreases or the risk profile of a market, industry, or group of customers changes materially, or if the allowance is determined to not be adequate, additional provisions for credit losses could be required, which could adversely affect our business, financial condition, liquidity, capital, and results of operations in future periods.

The allowance for loan and lease losses provides for probable losses that have been identified with specific valuation allowances for individually evaluated impaired loans and for probable losses believed to be inherent in the loan portfolio that have not been specifically identified. Internal risk ratings are assigned to each business loan at the time of approval and are subject to subsequent periodic reviews by the Corporation's senior management. The allowance for loan and lease losses is reviewed on a quarterly basis as part of the Corporation's continued evaluation of its asset quality. Refer to Critical Accounting Policies Allowance for Loan and Lease Losses section above for additional information about the methodology used by the Corporation to determine specific reserves and the general valuation allowance.

The Corporation continued to strengthen its reserve coverage for most portfolios. The allowance for loan losses to total loans for residential mortgage loans increased from 1.82% at December 31, 2010 to 2.19% as of March 31, 2011. The C&I loans reserve coverage ratio increased from 3.68% at December 31, 2010 to 4.17% at March 31, 2011. The construction loans reserve coverage ratio increased from 21.69% as of December 31, 2010 to 23.04% at March 31, 2011. In contrast, the commercial mortgage reserve coverage decreased from 6.32% at December 31, 2010 to 5.53% at March 31, 2011 due to decreases in non-performing loans, while the consumer and finance leases reserve coverage ratio decreased from 4.69% as of December 31, 2010 to 4.54% at March 31, 2011 due to decreases in non-performing loans.

Substantially all of the Corporation's loan portfolio is located within the boundaries of the U.S. economy. Whether the collateral is located in Puerto Rico, the U.S. and British Virgin Islands or the U.S. mainland (mainly in the state of Florida), the performance of the Corporation's loan portfolio and the value of the collateral supporting the transactions are dependent upon the performance of and conditions within each specific area real estate market. Economic reports related to the real estate market in Puerto Rico indicate that the real estate market experienced readjustments in value driven by the loss of income due to the unemployment of consumers, reduced demand and the general economic conditions. The Corporation sets adequate loan-to-value ratios upon original approval following its regulatory and credit policy standards. The real estate market for the U.S. Virgin Islands remains fairly stable. In the Florida market, residential real estate has experienced a very slow turnover, but the Corporation continues to reduce its credit exposure through disposition of assets and different loss mitigation initiatives.

As shown in the following table, the allowance for loan and lease losses increased to \$561.7 million at March 31, 2011, compared with \$553.0 million at December 31, 2010. The \$8.7 million increase in the allowance primarily reflected increases in specific reserves associated with C&I impaired loans. Refer to the Provision for Loan and Lease Losses discussion above for additional information.

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The following table sets forth an analysis of the activity in the allowance for loan and lease losses during the periods indicated:

(Dollars in thousands)	Quarter Ended March 31,	
	2011	2010
Allowance for loan and lease losses, beginning of period	\$ 553,025	\$ 528,120
Provision (recovery) for loan and lease losses:		
Residential mortgage	6,327	28,739
Commercial mortgage	13,381	37,560
Commercial and Industrial	41,486	(7,685)
Construction	22,463	99,300
Consumer and finance leases	5,075	13,051
Total provision for loan and lease losses	88,732	170,965
Charge-offs:		
Residential mortgage	(5,404)	(13,346)
Commercial mortgage	(31,171)	(19,318)
Commercial and Industrial	(16,344)	(23,922)
Construction	(19,165)	(53,323)
Consumer and finance leases	(11,969)	(16,397)
	(84,053)	(126,306)
Recoveries:		
Residential mortgage	243	
Commercial mortgage	67	21
Commercial and Industrial	56	146
Construction	1,927	108
Consumer and finance leases	1,698	2,249
	3,991	2,524
Net charge-offs	(80,062)	(123,782)
Allowance for loan and lease losses, end of period	\$ 561,695	\$ 575,303
Allowance for loan and lease losses to period end total loans receivable	5.06%	4.33%
Net charge-offs annualized to average loans outstanding during the period	2.74%	3.65%
Provision for loan and lease losses to net charge-offs during the period	1.11x	1.38x

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The following table sets forth information concerning the allocation of the allowance for loan and lease losses by loan category and the percentage of loan balances in each category to the total of such loans as of the dates indicated:

(In thousands)	As of March 31, 2011		As of December 31, 2010	
	Amount	Percent	Amount	Percent
Residential mortgage	\$ 63,496	26%	\$ 62,330	29%
Commercial mortgage loans	87,873	14%	105,596	14%
Construction loans	157,197	6%	151,972	6%
Commercial and Industrial loans (including loans to local financial institutions)	177,839	39%	152,641	36%
Consumer loans and finance leases	75,290	15%	80,486	15%
	\$ 561,695	100%	\$ 553,025	100%

The following table sets forth information concerning the composition of the Corporation's allowance for loan and lease losses as of March 31, 2011 and December 31, 2010 by loan category and by whether the allowance and related provisions were calculated individually or through a general valuation allowance:

(Dollars in thousands)	Residential Mortgage Loans	Commercial Mortgage Loans	C&I Loans	Construction Loans	Consumer and Finance Leases	Total
As of March 31, 2011						
Impaired loans without specific reserves:						
Principal balance of loans, net of charge-offs	\$ 293,488	\$ 18,628	\$ 63,328	\$ 37,910	\$ 1,141	\$ 414,495
Impaired loans with specific reserves:						
Principal balance of loans, net of charge-offs	272,782	213,426	332,651	327,502	1,266	1,147,627
Allowance for loan and lease losses	43,295	29,610	81,989	98,167	415	253,476
Allowance for loan and lease losses to principal balance	15.87%	13.87%	24.65%	29.97%	32.78%	22.09%
Loans with general allowance:						
Principal balance of loans	2,330,422	1,356,714	3,866,681	316,833	1,657,003	9,527,653
Allowance for loan and lease losses	20,201	58,263	95,850	59,030	74,875	308,219

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Allowance for loan and lease losses to principal balance	0.87%	4.29%	2.48%	18.63%	4.52%	3.23%
Total loans held for investment:						
Principal balance of loans	\$2,896,692	\$1,588,768	\$4,262,660	\$682,245	\$1,659,410	\$11,089,775
Allowance for loan and lease losses	63,496	87,873	177,839	157,197	75,290	561,695
Allowance for loan and lease losses to principal balance	2.19%	5.53%	4.17%	23.04%	4.54%	5.06%
As of December 31, 2010						
Impaired loans without specific reserves:						
Principal balance of loans, net of charge-offs	\$ 244,648	\$ 32,328	\$ 54,631	\$ 25,074	\$ 659	\$ 357,340
Impaired loans with specific reserves:						
Principal balance of loans, net of charge-offs	311,187	150,442	325,206	237,970	1,496	1,026,301
Allowance for loan and lease losses	42,666	26,869	65,030	57,833	264	192,662
Allowance for loan and lease losses to principal balance	13.71%	17.86%	20.00%	24.30%	17.65%	18.77%
Loans with general allowance:						
Principal balance of loans	2,861,582	1,487,391	3,771,927	437,535	1,713,360	10,271,795
Allowance for loan and lease losses	19,664	78,727	87,611	94,139	80,222	360,363
Allowance for loan and lease losses to principal balance	0.69%	5.29%	2.32%	21.52%	4.68%	3.51%
Total loans held for investment:						
Principal balance of loans	\$3,417,417	\$1,670,161	\$4,151,764	\$700,579	\$1,715,515	\$11,655,436
Allowance for loan and lease losses	62,330	105,596	152,641	151,972	80,486	553,025

Allowance for loan
and lease losses to
principal balance

1.82%

6.32%

85

3.68%

21.69%

4.69%

4.74%

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The following tables show the activity for impaired loans and the related specific reserves during the first quarter of 2011 and 2010:

	Quarter Ended	
	March 31, 2011	March 31, 2010
	(In thousands)	
Impaired Loans:		
Balance at beginning of period	\$ 1,383,641	\$ 1,656,264
Loans determined impaired during the period	277,548	317,333
Net charge-offs	(60,620)	(101,259)
Loans sold, net of charge-offs	(850)	(18,749)
Loans foreclosed, paid in full and partial payments or no longer considered impaired	(37,597)	(7,503)
Balance at end of period	\$ 1,562,122	\$ 1,846,086

For the Quarter Ended March 31, 2011

	Residential Mortgage Loans	Commercial Mortgage Loans	C&I Loans	Construction Loans	Consumer and Finance Leases	Total
Allowance for impaired loans, beginning of period	\$ 42,666	\$ 26,869	\$ 65,030	\$ 57,833	\$ 264	\$ 192,662
Provision for impaired loans	5,791	27,841	28,205	59,091	506	121,434
Charge-offs	(5,162)	(25,100)	(11,246)	(18,757)	(355)	(60,620)
Allowance for impaired loans, end of period	\$ 43,295	\$ 29,610	\$ 81,989	\$ 98,167	\$ 415	\$ 253,476

For the Quarter Ended March 31, 2010

	Residential Mortgage Loans	Commercial Mortgage Loans	C&I Loans	Construction Loans	Total
Allowance for impaired loans, beginning of period	\$ 2,616	\$ 30,945	\$ 62,491	\$ 86,093	\$ 182,145
Provision for impaired loans	9,137	31,362	33,655	90,260	164,414
Charge-offs	(9,778)	(17,429)	(21,738)	(53,314)	(102,259)
Allowance for impaired loans, end of period	\$ 1,975	\$ 44,878	\$ 74,408	\$ 123,039	\$ 244,300

Credit Quality

Credit quality performance in the 2011 first quarter continued to show signs of stabilization, including a \$5.9 million decrease in non-performing loans held for investment. Other key credit quality metrics showed

improvements, including continued improvement in construction and residential net charge-offs, and some noticeable improvement in C&I and consumer charge-offs. The allowance for loan and lease losses was further strengthened and increased \$8.7 million to \$561.7 million, or 5.06% of period-end total loans, from \$553.0 million, or 4.74% at December 31, 2010.

Non-performing Loans and Non-performing Assets

Total non-performing assets consist of non-performing loans, foreclosed real estate and other repossessed properties as well as non-performing investment securities. Non-performing loans are those loans on which the accrual of interest is discontinued. When a loan is placed in non-performing status, any interest previously recognized and not collected is reversed and charged against interest income.

Non-performing Loans Policy

Residential Real Estate Loans The Corporation classifies real estate loans in non-performing status when interest and principal have not been received for a period of 90 days or more.

Commercial and Construction Loans The Corporation places commercial loans (including commercial real estate and construction loans) in non-performing status when interest and principal have not been received for a period of 90 days or more or when collection of all of principal or interest is not expected due to deterioration in the financial condition of the borrower.

Finance Leases Finance leases are classified in non-performing status when interest and principal have not been received for a period of 90 days or more.

Consumer Loans Consumer loans are classified in non-performing status when interest and principal have not been received for a period of 90 days or more.

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Cash payments received on certain loans that are impaired and collateral dependent are recognized when collected in accordance with the contractual terms of the loans. The principal portion of the payment is used to reduce the principal balance of the loan, whereas the interest portion is recognized on a cash basis (when collected). However, when management believes that the ultimate collectability of principal is in doubt, the interest portion is applied to principal. The risk exposure of this portfolio is diversified as to individual borrowers and industries among other factors. In addition, a large portion is secured with real estate collateral.

Other Real Estate Owned (OREO)

OREO acquired in settlement of loans is carried at the lower of cost (carrying value of the loan) or fair value less estimated costs to sell off the real estate at the date of acquisition (estimated realizable value).

Other Repossessed Property

The other repossessed property category includes repossessed boats and autos acquired in settlement of loans. Repossessed boats and autos are recorded at the lower of cost or estimated fair value.

Investment Securities

This category presents investment securities reclassified to non-accrual status, at their book value.

Past Due Loans over 90 days and still accruing

These are accruing loans which are contractually delinquent 90 days or more. These past due loans are either current as to interest but delinquent in the payment of principal or are insured or guaranteed under applicable FHA and VA programs.

The Corporation has in place loan loss mitigation programs providing homeownership preservation assistance. Loans modified through this program are reported as non-performing loans and interest is recognized on a cash basis. When there is reasonable assurance of repayment and the borrower has made payments over a sustained period, the loan is returned to accrual status.

The following table presents non-performing assets as of the dates indicated:

(Dollars in thousands)	March 31, 2011	December 31, 2010
Non-performing loans held for investment:		
Residential mortgage	\$ 391,962	\$ 392,134
Commercial mortgage	129,828	217,165
Commercial and Industrial	327,477	317,243
Construction	341,179	263,056
Finance leases	3,632	3,935
Consumer	38,973	45,456
	1,233,051	1,238,989
Other real estate owned	91,948	84,897
Other repossessed property	15,125	14,023
Investment securities (1)	64,543	64,543
Total non-performing assets, excluding loans held for sale	\$ 1,404,667	\$ 1,402,452
Non-performing loans held for sale	5,454	159,321
Total non-performing assets, including loans held for sale	\$ 1,410,121	\$ 1,561,773

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Past due loans 90 days and still accruing	\$ 154,299	\$ 144,114
Non-performing assets to total assets	9.34%	9.96%
Non-performing loans held for investment to total loans held for investment	11.12%	10.63%
Allowance for loan and lease losses	561,695	553,025
Allowance to total non-performing loans held for investment	45.55%	44.64%
Allowance to total non-performing loans held for investment, excluding residential real estate loans	66.78%	65.30%

(1) Collateral pledged with Lehman Brothers Special Financing, Inc.

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The following table shows non-performing assets by geographic segment:

(Dollars in thousands)	March 31, 2011	December 31, 2010
Puerto Rico:		
Non-performing loans held for investment:		
Residential mortgage	\$ 335,919	\$ 330,737
Commercial mortgage	87,655	177,617
Commercial and Industrial	319,541	307,608
Construction	180,041	196,948
Finance leases	3,632	3,935
Consumer	36,648	43,241
Total non-performing loans held for investment	963,436	1,060,086
REO	70,416	67,488
Other repossessed property	14,949	13,839
Investment securities	64,543	64,543
Total non-performing assets, excluding loans held for sale	\$ 1,113,344	\$ 1,205,956
Non-performing loans held for sale	5,454	159,321
Total non-performing assets, including loans held for sale	\$ 1,118,798	\$ 1,365,277
Past due loans 90 days and still accruing	\$ 140,180	\$ 142,756
Virgin Islands:		
Non-performing loans held for investment:		
Residential mortgage	\$ 10,249	\$ 9,655
Commercial mortgage	8,233	7,868
Commercial and Industrial	5,572	6,078
Construction	117,153	16,473
Consumer	1,052	927
Total non-performing loans held for investment	142,259	41,001
REO	3,034	2,899
Other repossessed property	151	108
Total non-performing assets, excluding loans held for sale	\$ 145,444	\$ 44,008
Non-performing loans held for sale		
Total non-performing assets, including loans held for sale	\$ 145,444	\$ 44,008
Past due loans 90 days and still accruing	\$ 10,734	\$ 1,358

Florida:

Non-performing loans held for investment:		
Residential mortgage	\$ 45,794	\$ 51,742
Commercial mortgage	33,940	31,680
Commercial and Industrial	2,364	3,557
Construction	43,985	49,635
Consumer	1,273	1,288
Total non-performing loans held for investment	127,356	137,902
REO	18,498	14,510
Other repossessed property	25	76
Total non-performing assets, excluding loans held for sale	\$ 145,879	\$ 152,488
Non-performing loans held for sale		
Total non-performing assets, including loans held for sale	\$ 145,879	\$ 152,488
Past due loans 90 days and still accruing	\$ 3,385	\$

Total non-performing loans were \$1.24 billion as of March 31, 2011, down from \$1.40 billion at December 31, 2010. The completion of the loan sale transaction with a joint venture removed approximately \$153.6 million of non-performing loans and \$257 million of adversely classified assets from the balance sheet. Total non-performing loans held for investment, which exclude non-

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performing loans held for sale, were \$1.23 billion at March 31, 2011, which represented 11.12% of total loans held for investment. This was down \$5.9 million from December 31, 2010. The decrease in non-performing loans held for investment from the fourth quarter of 2010 primarily reflected declines in commercial mortgage and consumer non-performing loans, partially offset by increases in construction and C&I non-performing loans.

Non-performing commercial mortgage loans held for investment decreased by \$87.3 million, or 40%, from the end of the fourth quarter of 2010. This decline was substantially related to a \$85.6 million loan relationship in Puerto Rico which was formally restructured so as to be reasonably assured of principal and interest repayment and of performance according to its modified terms. The Corporation restructured the balance due from this borrower by splitting it into two separate notes. Non-performing commercial mortgage loans increased \$2.3 million and \$0.4 million in the United States and Virgin Islands, respectively.

Non-performing construction loans held for investment increased by \$78.1 million, or 30%, from the end of the fourth quarter of 2010. The increase mainly reflected the placement in non-performing status of a \$100 million loan relationship related to a commercial project in the Virgin Islands region, which was the single largest construction relationship in performing status prior to this quarter. This was partially offset by charge-offs and paydowns. Non-performing construction loans held for investment in Puerto Rico decreased \$16.9 million mainly due to charge-offs and paydowns while the non-performing construction loan portfolio in the United States decreased by \$5.7 million. The decrease in non-performing construction loans in the United States portfolio was also mainly related to charge-offs, including \$3.0 million associated with a residential development project. There were no inflows of construction projects into non-accrual status in Puerto Rico and the United States during the first quarter of 2011.

C&I non-performing loans held for investment increased by \$10.2 million, or 3%, on a sequential quarter basis. The increase was related primarily to one relationship in Puerto Rico of approximately \$7.9 million. This was partially offset by charge-offs, including a \$5.0 million charge-off in one relationship in Puerto Rico. In the United States and the Virgin Islands, C&I non-performing loans decreased by \$1.2 million and \$0.5 million, respectively. The decrease in the United States was mainly related to the sale of a \$0.9 million loan.

Non-performing residential mortgage loans remained relatively flat at \$392 million. In Puerto Rico, non-performing residential mortgage loans increased by \$5.2 million. Meanwhile, non-performing residential mortgage loans decreased by \$5.9 million in the United States, including \$4.1 million related to loans foreclosed. In the Virgin Islands, non-performing residential mortgage loans increased by \$0.6 million. Approximately \$231.0 million, or 59% of total non-performing residential mortgage loans, have been written down to their net realizable value.

The levels of non-performing consumer loans, including finance leases, showed a \$6.8 million decrease during the first quarter, mainly related to auto financings in Puerto Rico.

At March 31, 2011, approximately \$282.1 million of the loans placed in non-accrual status, mainly construction and commercial loans, were current, or had delinquencies of less than 90 days in their interest payments, including \$68.9 million of restructured loans maintained in nonaccrual status until the restructured loans meet the criteria of sustained payment performance under the revised terms for reinstatement to accrual status. Collections are being recorded on a cash basis through earnings, or on a cost-recovery basis, as conditions warrant.

During the quarter ended March 31, 2011, interest income of approximately \$1.8 million related to non-performing loans with a carrying value of \$661.8 million as of March 31, 2011, mainly non-performing construction and commercial loans, was applied against the related principal balances under the cost-recovery method.

As of March 31, 2011, approximately \$369.7 million, or 30%, of total non-performing loans held for investment have been charged-off to their net realizable value.

The allowance to non-performing loans held for investment ratio as of March 31, 2011 was 45.55%, compared to 44.64% as of December 31, 2010. As of March 31, 2011, approximately \$369.7 million, or 30%, of total non-performing loans have been charged-off to their net realizable value as shown in the following table.

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(Dollars in thousands)	Residential Mortgage Loans	Commercial Mortgage Loans	C&I Loans	Construction Loans	Consumer and Finance Leases	Total
As of March 31, 2011						
Non-performing loans held for investment charged-off to realizable value	\$ 231,039	\$ 11,240	\$ 75,475	\$ 50,804	\$ 1,141	\$ 369,699
Other non-performing loans held for investment	160,923	118,588	252,002	290,375	41,464	863,352
Total non-performing loans held for investment	\$ 391,962	\$ 129,828	\$ 327,477	\$ 341,179	\$ 42,605	\$ 1,233,051
Allowance to non-performing loans held for investment	16.20%	67.68%	54.31%	46.07%	176.72%	45.55%
Allowance to non-performing loans held for investment, excluding non-performing loans charged-off to realizable value	39.46%	74.10%	70.57%	54.14%	181.58%	65.06%
As of December 31, 2010						
Non-performing loans held for investment charged-off to realizable value	\$ 291,118	\$ 20,239	\$ 101,151	\$ 32,139	\$ 659	\$ 445,306
Other non-performing loans held for investment	101,016	196,926	216,092	230,917	48,732	793,683
Total non-performing loans held for investment	\$ 392,134	\$ 217,165	\$ 317,243	\$ 263,056	\$ 49,391	\$ 1,238,989
Allowance to non-performing loans held for investment	15.90%	48.62%	48.11%	57.77%	162.96%	44.64%
Allowance to non-performing loans held for investment, excluding non-performing loans charged-off to realizable value	61.70%	53.62%	70.64%	65.81%	165.16%	69.68%

The Corporation provides homeownership preservation assistance to its customers through a loss mitigation program in Puerto Rico and through programs sponsored by the Federal Government. Depending upon the nature of borrowers' financial condition, restructurings or loan modifications through this program as well as other restructurings

of individual commercial, commercial mortgage, construction and residential mortgage loans in the U.S. mainland fit the definition of TDR. A restructuring of a debt constitutes a TDR if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider.

Modifications involve changes in one or more of the loan terms that bring a defaulted loan current and provide sustainable affordability. Changes may include the refinancing of any past-due amounts, including interest and escrow, the extension of the maturity of the loan and modifications of the loan rate. As of March 31, 2011, the Corporation's TDR loans consisted of \$291.2 million of residential mortgage loans, \$40.7 million commercial and industrial loans, \$139.9 million commercial mortgage loans and \$15.4 million of construction loans. Outstanding unfunded loan commitments on TDR loans amounted to \$1.2 million as of March 31, 2011.

Included in the \$139.9 million of commercial mortgage TDR loans are certain loan relationships restructured through loan splitting, one in the first quarter of 2011 and one in the fourth quarter of 2010. Each of these loan relationships were restructured into two notes; one that represents the portion of the loan that is expected to be fully collected along with contractual interest and the second note that represents the portion of the original loan that was charged-off. The renegotiations of these loans have been made after analyzing the borrowers' and guarantors capacity to repay the debt and ability to perform under the modified terms. For the relationship restructured in the first quarter of 2011, the first note of \$57.5 million was placed on a monthly payment that amortize the debt over 30 years at a market rate of interest. The second note, amounting to \$28.3 million was fully charged-off. For the relationship restructured in the fourth quarter of 2010, as part of the renegotiation of the loans, the first note of \$17 million was placed on a monthly payment schedule that amortizes the debt over 30 years at a market rate of interest. The second note for \$2.7 million was fully charged-off. The following tables provide additional information about the volume of this type of loan restructurings and the effect on the allowance for loan and lease losses in 2011.

Principal balance deemed collectible at end of period	\$ 74,442
Amount charged-off during the first quarter of 2011	\$ 28,340
Allowance for loan losses:	
Balance at beginning of period	\$ 23,108
Provision for loan losses	7,205
Charge-offs	(28,340)
Balance at end of period	\$ 1,973

The loans comprising the \$74.4 million that have been deemed collectible were placed in accruing status as the borrowers have exhibited a period of sustained performance but continue to be individually evaluated for impairment purposes. These transactions contributed to a \$105.3 million decrease in non-performing loans over the last two quarters.

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The REO portfolio, which is part of non-performing assets, increased by \$7.1 million, reflecting increases in residential properties in the United States, and increases in both commercial and residential properties in Puerto Rico, partially offset by sales of REO properties. Consistent with the Corporation's assessment of the value of properties and current and future market conditions, management continues to execute strategies to dispose real estate acquired in satisfaction of debt. During the first quarter of 2011, the Corporation sold approximately \$12.6 million of REO properties (\$3.5 million in Florida, \$8.8 million in Puerto Rico and \$0.3 million in the Virgin Islands), compared to \$6.0 million in the first quarter of 2010.

The over 90-day delinquent, but still accruing, loans held for investment, excluding loans guaranteed by the U.S. Government, increased during the first quarter of 2011 by \$7.1 million to \$69.9 million, or 0.63% of total loans held for investment, at March 31, 2011.

Net Charge-offs and Total Credit Losses

Total net charge-offs for the first quarter of 2011 were \$80.1 million, or 2.74% of average loans on an annualized basis. This was down \$43.7 million, or 35%, from \$123.8 million, or an annualized 3.65%, in the first quarter of 2010. Lower net charge-offs were reflected primarily in the Puerto Rico and the United States portfolio with a \$9.8 million and a \$33.6 million decrease, respectively, mainly related to the construction and residential mortgage loan portfolio. Net charge-offs in Virgin Islands remained relatively flat reflecting a \$0.4 million decrease.

Construction loans net charge-offs in the first quarter of 2011 were \$17.2 million, or an annualized 8.50%, down from \$53.2 million, or an annualized 14.35% of related loans, in the first quarter of 2010. Approximately 70%, or \$12.0 million, of the construction loan net charge-offs in the first quarter of 2011 were related to the Puerto Rico portfolio, driven by three relationships with charge-offs totaling \$10.9 million associated with commercial and residential projects. In Florida, construction loan net charge-offs were \$5.2 million, a decrease of \$14.3 million when compared to 2010 first quarter levels, of which approximately \$4.7 million was related to two relationships. The construction portfolio in Florida has been reduced to \$70.4 million, as of March 31, 2011, from \$78.5 million, as of December 31, 2010. Construction loans net charge-offs in the Virgin Islands were \$0.1 million for the first quarter of 2011, unchanged from the first quarter of 2010. Construction loans charge-offs in the Virgin Islands over the last two quarters are directly related to an adequately reserved residential project placed in non-accruing status in the fourth quarter of 2010.

C&I loan net charge-offs in the first quarter of 2011 were \$16.3 million, or an annualized 1.54% of related average loans, down from \$23.8 million, or an annualized 1.88% of related loans, in the first quarter of 2010. Approximately 95%, or \$15.4 million, of net charge-offs in the first quarter of 2011, were in Puerto Rico, of which \$10.1 million was related to four relationships. No significant C&I loans charge-offs were recorded in the United States or Virgin Islands portfolios.

Residential mortgage loan net charge-offs were \$5.2 million, or an annualized 0.63% of related average loans. This represents a decrease of \$8.1 million from \$13.3 million, or an annualized 1.50% of related average balances in the first quarter of 2011. Although there continues to be valuation pressure, the Corporation experienced reductions in delinquent loans. Approximately \$4.0 million in charge-offs for the first quarter of 2011 (\$1.7 million in Puerto Rico and \$2.3 million in Florida) resulted from valuations for impairment purposes of residential mortgage loan portfolios considered homogeneous given high delinquency and loan-to-value levels, compared to \$9.8 million recorded in the first quarter of 2010. The total amount of the residential mortgage loan portfolio that has been charged-off to its net realizable value as of March 31, 2011 amounted to \$231.0 million. This represents approximately 53% of the total non-performing residential mortgage loan portfolio outstanding as of March 31, 2011. Net charge-offs of residential mortgage loans also include \$1.4 million related to loans foreclosed during the first quarter of 2011, down from \$3.3 million recorded for loans foreclosed in the first quarter of 2010. Loss rates in the Corporation's Puerto Rico operations continue to be lower than loss rates in the Florida market.

Net charge-offs on consumer loan and finance leases in the first quarter of 2011 were \$10.3 million, or an annualized 2.43% of related average loans, compared to \$14.1 million, or an annualized 3.01% of average loans for the first quarter of 2010.

Commercial mortgage loan net charge-offs in the first quarter of 2011 were \$31.1 million, or an annualized 7.37% of related average loans, up from \$19.3 million, or an annualized 4.85% of related loans, in the first quarter of 2010.

The 2011 first quarter net charge-offs were mainly driven by the charge-off related to the aforementioned \$85.6 million relationship in Puerto Rico restructured by the Corporation through a loan split. Commercial mortgage loan net charge-offs in Florida amounted to \$1.9 million for the first quarter of 2011.

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The following table presents annualized charge-offs to average loans held-in-portfolio:

	Quarter Ended	
	March 31, 2011	March 31, 2010
Residential mortgage	0.63%	1.50%
Commercial mortgage	7.37%	4.85%
Commercial and Industrial	1.54%	1.88%
Construction	8.50%	14.35%
Consumer and finance leases	2.43%	3.01%
Total loans	2.74%	3.65%

The above ratios are based on annualized charge-offs and are not necessarily indicative of the results expected for the entire year or in subsequent periods.

The following table presents annualized net charge-offs to average loans by geographic segment:

	Quarter Ended	
	March 31, 2011	March 31, 2010
PUERTO RICO:		
Residential mortgage	0.39%	1.11%
Commercial mortgage	10.07%	0.71%
Commercial and Industrial	1.55%	1.92%
Construction	8.77%	13.45%
Consumer and finance leases	2.50%	2.95%
Total loans	2.82%	2.80%
VIRGIN ISLANDS:		
Residential mortgage	0.05%	0.47%
Commercial mortgage	0.00%	0.00%
Commercial and Industrial	1.59%	(0.02)% (1)
Construction	0.16%	0.15%
Consumer and finance leases	1.05%	3.82%
Total loans	0.45%	0.55%
FLORIDA:		
Residential mortgage	3.26%	5.70%
Commercial mortgage	1.65%	13.23%
Commercial and Industrial	0.92%	10.78%
Construction	26.29%	27.23%
Consumer and finance leases	1.59%	3.96%
Total loans	4.29%	13.90%

(1) For the first quarter of 2010, recoveries in commercial and industrial loans in the Virgin Islands exceeded charge-offs.

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Total credit losses (equal to net charge-offs plus losses on REO operations) for the first quarter ended March 31, 2011 amounted to \$85.6 million, or 2.91% on an annualized basis to average loans and repossessed assets in contrast to credit losses of \$127.5 million, or a loss rate of 3.84%, for the first quarter of 2010.

The following table presents a detail of the REO inventory and credit losses for the periods indicated:

	Quarter Ended March 31,	
	2011	2010
	(In thousands)	
REO		
REO balances, carrying value:		
Residential	\$ 58,426	\$ 38,851
Commercial	26,434	20,322
Condo-conversion projects		8,000
Construction	7,088	6,271
Total	\$ 91,948	\$ 73,444
REO activity (number of properties):		
Beginning property inventory,	479	285
Properties acquired	91	98
Properties disposed	(80)	(52)
 Ending property inventory	 490	 331
Average holding period (in days)		
Residential	332	235
Commercial	418	204
Condo-conversion projects		733
Construction	480	417
	368	296
REO operations (loss) gain:		
Market adjustments and (losses) gain on sale:		
Residential	(2,633)	(1,245)
Commercial	(1,103)	(676)
Condo-conversion projects		
Construction	135	49
	(3,601)	(1,872)
 Other REO operations expenses	 (1,899)	 (1,821)
 Net Loss on REO operations	 \$ (5,500)	 \$ (3,693)

CHARGE-OFFS

Residential charge-offs, net	(5,161)	(13,346)
Commercial charge-offs, net	(47,392)	(43,073)
Construction charge-offs, net	(17,238)	(53,215)
Consumer and finance leases charge-offs, net	(10,271)	(14,148)
Total charge-offs, net	(80,062)	(123,782)

TOTAL CREDIT LOSSES (1)	\$ (85,562)	\$ (127,475)
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LOSS RATIO PER CATEGORY (2):

Residential	0.94%	1.62%
Commercial	3.27%	2.63%
Construction	8.36%	14.21%
Consumer	2.41%	3.00%
TOTAL CREDIT LOSS RATIO (3)	2.91%	3.84%

(1) Equal to REO operations (losses) gains plus Charge-offs, net.

(2) Calculated as net charge-offs plus market adjustments and gains (losses) on sale of REO divided by average loans and repossessed assets.

(3) Calculated as net charge-offs plus net loss on REO operations divided by average loans and repossessed assets.

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Operational Risk

The Corporation faces ongoing and emerging risk and regulatory pressure related to the activities that surround the delivery of banking and financial products. Coupled with external influences such as market conditions, security risks, and legal risk, the potential for operational and reputational loss has increased. In order to mitigate and control operational risk, the Corporation has developed, and continues to enhance, specific internal controls, policies and procedures that are designated to identify and manage operational risk at appropriate levels throughout the organization. The purpose of these mechanisms is to provide reasonable assurance that the Corporation's business operations are functioning within the policies and limits established by management.

The Corporation classifies operational risk into two major categories: business specific and corporate-wide affecting all business lines. For business specific risks, a risk assessment group works with the various business units to ensure consistency in policies, processes and assessments. With respect to corporate-wide risks, such as information security, business recovery, and legal and compliance, the Corporation has specialized groups, such as the Legal Department, Information Security, Corporate Compliance, Information Technology and Operations. These groups assist the lines of business in the development and implementation of risk management practices specific to the needs of the business groups.

Legal and Compliance Risk

Legal and compliance risk includes the risk of non-compliance with applicable legal and regulatory requirements, the risk of adverse legal judgments against the Corporation, and the risk that a counterparty's performance obligations will be unenforceable. The Corporation is subject to extensive regulation in the different jurisdictions in which it conducts its business, and this regulatory scrutiny has been significantly increasing over the last several years. The Corporation has established and continues to enhance procedures based on legal and regulatory requirements that are designed to ensure compliance with all applicable statutory and regulatory requirements. The Corporation has a Compliance Director who reports to the Chief Risk Officer and is responsible for the oversight of regulatory compliance and implementation of an enterprise-wide compliance risk assessment process. The Compliance division has officer roles in each major business areas with direct reporting relationships to the Corporate Compliance Group.

Concentration Risk

The Corporation conducts its operations in a geographically concentrated area, as its main market is Puerto Rico. However, the Corporation has diversified its geographical risk as evidenced by its operations in the Virgin Islands and in Florida.

As of March 31, 2011, the Corporation had \$325.9 million outstanding of credit facilities granted to the Puerto Rico Government and/or its political subdivisions compared to \$325.1 million as of December 31, 2010, and \$98.8 million granted to the Virgin Islands government, compared to \$84.3 million as of December 31, 2010. A substantial portion of these credit facilities are obligations that have a specific source of income or revenues identified for their repayment, such as property taxes collected by the central Government and/or municipalities. Another portion of these obligations consists of loans to public corporations that obtain revenues from rates charged for services or products, such as electric power utilities. Public corporations have varying degrees of independence from the central Government and many receive appropriations or other payments from it. The Corporation also has loans to various municipalities in Puerto Rico for which the good faith, credit and unlimited taxing power of the applicable municipality have been pledged to their repayment.

Aside from loans extended to the Puerto Rico Government and its political subdivisions, the largest loan to one borrower as of March 31, 2011 in the amount of \$285.4 million is with one mortgage originator in Puerto Rico, Doral Financial Corporation. This commercial loan is secured by individual real-estate loans, mostly 1-4 residential mortgage loans.

Of the total gross loan held for investment portfolio of \$11.1 billion as of March 31, 2011, approximately 83% have credit risk concentration in Puerto Rico, 8% in the United States and 9% in the Virgin Islands.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For information regarding market risk to which the Corporation is exposed, see the information contained in Part I Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations - Risk Management.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Control and Procedures

First BanCorp's management, including its Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of First BanCorp's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of March 31, 2011. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective.

Internal Control over Financial Reporting

There have been no changes to the Corporation's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

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PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In the opinion of the Company's management, the pending and threatened legal proceedings of which management is aware will not have a material adverse effect on the financial condition, results of operations or cash flows of the Corporation.

ITEM 1A. RISK FACTORS

Our business, operating results and/or the market price of our common and preferred stock may be significantly affected by a number of factors. For a detailed discussion of certain risk factors that could affect the Corporation's operations, financial condition or results for future periods see Item 1A, Risk Factors, in the Corporation's 2010 Annual Report on Form 10-K. These factors could also cause actual results to differ materially from historical results or the results contemplated by the forward-looking statements contained in this report. Also refer to the discussion in Part I Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations in this report for additional information that may supplement or update the discussion of risk factors in the Corporation's 2010 Form 10-K.

The risks described in the Corporation's 2010 Form 10-K are not the only risks facing the Corporation. Additional risks and uncertainties not currently known to the Corporation or currently deemed by the Corporation to be immaterial also may materially adversely affect the Corporation's business, financial condition or results of operations.

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

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. RESERVED

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

12.1 Ratio of Earnings to Fixed Charges.

12.2 Ratio of Earnings to Fixed Charges and Preference Dividends.

31.1 CEO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 CFO Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 CEO Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 CFO Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Corporation has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized:

First BanCorp.
Registrant

Date: May 16, 2011

By: /s/ Aurelio Alemán
Aurelio Alemán
President and
Chief Executive Officer

Date: May 16, 2011

By: /s/ Orlando Berges
Orlando Berges
Executive Vice President
and Chief Financial Officer

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LEFT: 0pt; TEXT-INDENT: 36pt; MARGIN-RIGHT: 0pt" align="justify">All of the Company's Agency MBS are classified as available-for-sale, and substantially all of the Company's Agency MBS are pledged as collateral against repurchase agreements.

Securitized Mortgage loans. Securitized mortgage loans consist of loans pledged to support the repayment of securitization financing bonds issued by the Company. Securitized mortgage loans are reported at amortized cost. An allowance has been established for currently existing estimated losses on such loans. Securitized mortgage loans can only be sold subject to the lien of the respective securitization financing indenture.

Investment in Joint Venture. The Company accounts for its investment in joint venture using the equity method as it does not exercise control over significant asset decisions such as buying, selling or financing nor is it the primary beneficiary under FIN 46(R). Under the equity method, the Company increases its investment for its proportionate share of net income and contributions to the joint venture and decreases its investment balance by recording its proportionate share of net loss and distributions.

The Company periodically reviews its investment in joint venture for other than temporary declines in market value. Any decline that is not expected to be recovered in the next twelve months is considered other than temporary, and an impairment charge is recorded as a reduction to the carrying value of the investment.

Other Investments. Other investments include non-Agency MBS and equity securities, unsecuritized delinquent property tax receivables, and unsecuritized single-family and commercial mortgage loans. The unsecuritized delinquent property tax receivables and mortgage loans are carried at amortized cost. Non-agency MBS and equity securities are considered available-for-sale and are reported at fair value, with unrealized gains and losses excluded from earnings and reported as accumulated other comprehensive income.

Other investments also include real estate owned acquired through, or in lieu of, foreclosure in connection with the servicing of the delinquent tax lien receivables portfolio. Such investments are considered held for sale and are initially recorded at fair value less cost to sell (net realizable value) at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, management periodically performs valuations and adjusts the property to the lower

of cost or net realizable value. Revenue and expenses related to and changes in the valuation of the real estate owned are included in other income (expense).

Interest Income. Interest income is recognized when earned according to the terms of the underlying investment and when, in the opinion of management, it is collectible. For loans, the accrual of interest is discontinued when, in the opinion of management, the interest is not collectible in the normal course of business, when the loan is significantly past due or when the primary servicer of the loan fails to advance the interest and/or

principal due on the loan. For securities and other investments, the accrual of interest is discontinued when, in the opinion of management, it is probable that all amounts contractually due will not be collected. Loans are considered past due when the borrower fails to make a timely payment in accordance with the underlying loan agreement, inclusive of all applicable cure periods. All interest accrued but not collected for investments that are placed on a non-accrual status or are charged-off is reversed against interest income. Interest on these investments is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual status. Investments are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Premiums, Discounts, Debt Issuance Costs and Hedging Basis Adjustments

Premiums and discounts on investments and obligations are amortized into interest income or expense, respectively, over the life of the related investment or obligation using the effective yield method in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 91, “Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases.”

Repurchase Agreements

The Company uses repurchase agreements to finance certain of its investments. Under these repurchase agreements, the Company sells the securities to a lender and agrees to repurchase the same securities in the future for a price that is higher than the original sales price. The difference between the sale price that the Company receives and the repurchase price that the Company pays represents interest paid to the lender. Although structured as a sale and repurchase obligation, a repurchase agreement operates as a financing, in accordance with the provision of SFAS 140, under which the Company pledges its securities as collateral to secure a loan, which is equal in value to a specified percentage of the estimated fair value of the pledged collateral. The Company retains beneficial ownership of the pledged collateral. At the maturity of a repurchase agreement, the Company is required to repay the loan and concurrently receives back its pledged collateral from the lender or, with the consent of the lender, the Company may renew the agreement at the then prevailing financing rate. These repurchase agreements may require the Company to pledge additional assets to the lender in the event the estimated fair value of the existing pledged collateral declines.

Derivative Financial Instruments

The Company may enter into interest rate swap agreements, interest rate cap agreements, interest rate floor agreements, financial forwards, financial futures and options on financial futures (“Interest Rate Agreements”) to manage its sensitivity to changes in interest rates. These interest rate agreements are intended to provide income and cash flow to offset potential reduced net interest income and cash flow under certain interest rate environments. At the inception of an Interest Rate Agreement, these instruments are designated as either hedge positions or trading positions using criteria established in SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities” (as amended). If, at the inception of an Interest Rate Agreement, formal documentation is prepared that describes the risk being hedged, identifies the hedging instrument and the means to be used for assessing the effectiveness of the hedge and if it can be demonstrated that the hedging instrument will be highly effective at hedging the risk exposure, the derivative instrument will be designated as a cash flow hedge position. Otherwise, an Interest Rate Agreement will be classified as a trading position.

For Interest Rate Agreements designated as cash flow hedges, the Company evaluates the effectiveness of these hedges against the financial instrument being hedged. The effective portion of the hedge relationship on an interest rate agreement designated as a cash flow hedge is reported in accumulated other comprehensive income, and the ineffective portion of such hedge is reported in income. Amounts in accumulated other comprehensive income are reclassified into earnings in the same period during which the hedged transaction affects earnings. Derivative

instruments are carried at fair value in the financial statements of the Company.

As a part of the Company's interest rate risk management process, the Company may be required periodically to terminate hedge instruments. Any basis adjustments or changes in the fair value of hedges recorded in other comprehensive income are recognized into income or expense in conjunction with the original hedge or hedged exposure.

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If the underlying asset, liability or commitment is sold or matures, the hedge is deemed partially or wholly ineffective, or the criteria that was executed at the time the hedge instrument was entered into no longer exists, the interest rate agreement no longer qualifies as a designated hedge. Under these circumstances, such changes in the market value of the Interest Rate Agreement are recognized in current income.

For Interest Rate Agreements classified as a trading position, realized and unrealized changes in fair value of these instruments are recognized in the consolidated statements of operations as trading income or loss in the period in which the changes occur or when such trade instruments are settled. Amounts receivable from counter-parties, if any, are included on the consolidated balance sheets in other assets.

Cash Equivalents

Cash and cash equivalents include cash on hand and highly liquid investments with original maturities of three months or less.

Net Income Per Common Share

Net income per common share is presented on both a basic net income per common share and diluted net income per common share basis. Diluted net income per common share assumes the conversion of the convertible preferred stock into common stock, using the two-class method, and stock options, using the treasury stock method, but only if these items are dilutive. Each share of preferred stock is convertible into one share of common stock.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Actual results could differ from those estimates. The primary estimates inherent in the accompanying consolidated financial statements are discussed below.

Fair Value. On January 1, 2008, the Company adopted SFAS No. 157, "Fair Value Measurements" ("SFAS 157"), which defines fair value, provides a framework for measuring fair value and sets forth the disclosures required with respect to fair value measurements. Pursuant to SFAS 157, the fair value is the exchange price in an orderly transaction, that is not a forced liquidation or distressed sale, between market participants to sell an asset or transfer a liability in the market in which the reporting entity would transact for the asset or liability, that is, the principal or most advantageous market for the asset/liability. The transaction to sell the asset or transfer the liability is a hypothetical transaction at the measurement date, considered from the perspective of a market participant that holds the asset/liability. SFAS 157 provides a consistent definition of fair value which focuses on exit price and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs. In addition, SFAS 157 provides a framework for measuring fair value and establishes a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date.

The three levels of valuation hierarchy established by SFAS 157 are as follows:

- Level 1 — Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date. The Company's investments included in Level 1 fair value generally are equity securities listed in active markets.
-

Level 2 — Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life. Fair valued assets and liabilities that are generally included in this category are Agency MBS, which are valued based on the average of multiple dealer quotes that are active in the Agency MBS market.

- Level 3 — Inputs reflect management’s best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model. Generally, assets and liabilities carried at fair value and included in this category are non-agency mortgage-backed securities, delinquent property tax receivables and the obligation under payment agreement liability.

Estimates of fair value for financial instruments are based primarily on management’s judgment. Since the fair value of the Company’s financial instruments is based on estimates, actual fair values recognized may differ from those estimates recorded in the consolidated financial statements. The fair value of all financial instruments is presented in Note 11.

The Company accounts for its Agency MBS and non-Agency MBS in accordance with SFAS No. 115, “Accounting for Certain Investments in Debt and Equity Securities,” which requires that investments in debt and equity securities be designated as either “held-to-maturity,” “available-for-sale” or “trading” at the time of acquisition. All of the Company’s securities are designated as available-for-sale and are carried at their fair value with unrealized gains and losses excluded from earnings and reported in other comprehensive (loss)/income, a component of Shareholders’ Equity. The Company determines the fair value of its investment securities based upon prices obtained from a third-party pricing service and broker quotes. The Company applies the guidance prescribed in Financial Accounting Standards Board Staff Position SFAS 115-1 and SFAS 124-1, “The Meaning of Other-Than-Temporary Impairment and its Application to Certain Investments” in determining whether an other than temporary impairment has occurred.

Although the Company generally intends to hold its investment securities until maturity, it may, from time to time, sell any of its securities as part of the overall management of its business. The available-for-sale designation provides the Company with the flexibility to sell any of its investment securities. Upon the sale of an investment security, any unrealized gain or loss is reclassified out of accumulated other comprehensive (loss)/income to earnings as a realized gain or loss using the specific identification method.

Allowance for Loan Losses. An allowance for loan losses has been estimated and established for currently existing probable losses for loans in the Company’s investment portfolio that are considered impaired. Factors considered in establishing an allowance include current loan delinquencies, historical cure rates of delinquent loans, and historical and anticipated loss severity of the loans as they are liquidated. The factors differ by loan type (e.g., single-family versus commercial) and collateral type (e.g., multifamily versus office property). The allowance for losses is evaluated and adjusted periodically by management based on the actual and estimated timing and amount of probable credit losses, using the above factors, as well as industry loss experience. Where loans are considered homogeneous, the allowance for losses are established and evaluated on a pool basis. Otherwise, the allowance for losses is established and evaluated on a loan-specific basis. Provisions made to increase the allowance are charged as a current period expense. Single-family loans are considered impaired when they are 60 days past due. Commercial mortgage loans are evaluated on an individual basis for impairment. Commercial mortgage loans are secured by income-producing real estate and are evaluated for impairment when the debt service coverage ratio on the loan is less than 1:1 or when the loan is delinquent. Certain of the commercial mortgage loans are covered by loan guarantees that limit the Company’s exposure on these loans.

Loans secured by low-income housing tax credit properties account for 88% of the Company’s securitized commercial mortgage loan portfolio. Section 42 of the Code provides tax credits to investors in projects to construct or substantially rehabilitate properties that provide housing for qualifying low income families. Failure to comply with certain income and rental restrictions required by Section 42 or default on a loan financing a Section 42 property during the compliance period can result in the recapture of previously received tax credits. The potential cost of tax credit recapture provides an incentive to the property owner to support the property during the compliance period.

Other-than-Temporary Impairments. The Company evaluates all securities in its investment portfolio for other-than-temporary impairments. A security is generally defined to be other-than-temporarily impaired if, for a period of three consecutive quarters, the carrying value of such security exceeds its estimated fair value, and the Company estimates, based on projected future cash flows or other fair value determinants, that the fair value will remain below the carrying value for the foreseeable future. If an other-than-temporary impairment is deemed to exist, the Company records an impairment charge to adjust the carrying value of the security down to its estimated fair value. In certain instances, as a result of the other-than-temporary impairment analysis, the recognition or accrual of interest will be discontinued and the security will be placed on non-accrual status. Securities normally are not placed on non-accrual status if the servicer continues to advance on the impaired loans in the security.

The Company considers an investment to be impaired if the fair value of the investment is less than its recorded cost basis. Impairments of other investments are generally considered to be other-than-temporary when the fair value remains below the carrying value for three consecutive quarters. If the impairment is determined to be other-than-temporary, an impairment charge is recorded in order to adjust the carrying value of the investment to its estimated value.

Mortgage Servicing Rights. The Company retains the primary servicing rights for certain of its loans originated in prior years and subcontracts the performance of the primary servicing to unrelated third parties. The Company adopted SFAS No. 156, "Accounting for Servicing of Financial Assets – An Amendment of FASB Statement No. 140" on January 1, 2007, and now accounts for its mortgage servicing rights at fair value with changes in fair value reported in earnings.

Contingencies. In the normal course of business, there are various lawsuits, claims, and contingencies pending against the Company. In accordance with SFAS No. 5, "Accounting for Contingencies," we evaluate whether to establish provisions for estimated losses from pending claims, investigations and proceedings. Although the ultimate outcome of the various matters cannot be ascertained at this point, it is the opinion of management, after consultation with counsel, that the resolution of the foregoing matters will not have a material adverse effect on the financial condition of the Company, taken as a whole, such resolution may, however, have a material effect on the results of operations or cash flows in any future period, depending on the level of income for such period.

Securitization Transactions

The Company has securitized mortgage loans in a securitization transaction by transferring financial assets to a wholly owned trust, and the trust issues non-recourse securitization financing bonds pursuant to an indenture. Generally, the Company retains some form of control over the transferred assets, and/or the trust is not deemed to be a qualified special purpose entity. In instances where the trust is deemed not to be a qualified special purpose entity, the trust is included in the consolidated financial statements of the Company. For accounting and tax purposes, the loans and securities financed through the issuance of bonds in a securitization financing transaction are treated as assets of the Company (presented as securitized mortgage loans), and the associated bonds issued are treated as debt of the Company as securitization financing. The Company may retain certain of the bonds issued by the trust, and the Company has generally transferred collateral in excess of the bonds issued. This excess is typically referred to as over-collateralization. Each securitization trust generally provides the Company the right to redeem, at its option, the remaining outstanding bonds prior to their maturity date.

Recent Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board ("FASB") issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements, an amendment of ARB No. 51" ("SFAS 160"). SFAS 160 addresses reporting requirements in the financial statements of non-controlling interests to their equity share of subsidiary

investments. SFAS 160 applies to reporting periods beginning after December 15, 2008. The Company does not believe this pronouncement will have a material effect on its financial statements.

In December 2007, the FASB issued SFAS No. 141(R), "Business Combinations" ("SFAS 141(R)") which revised SFAS No. 141, "Business Combinations." This pronouncement is effective as of January 1, 2009. Under SFAS No. 141, organizations utilized the announcement date as the measurement date for the purchase price of the

acquired entity. SFAS 141(R) requires measurement at the date the acquirer obtains control of the acquiree, generally referred to as the acquisition date. SFAS 141(R) will have a significant impact on the accounting for transaction costs, restructuring costs, as well as the initial recognition of contingent assets and liabilities assumed during a business combination. Under SFAS 141(R), adjustments to the acquired entity's deferred tax assets and uncertain tax position balances occurring outside the measurement period are recorded as a component of the income tax expense, rather than goodwill. As the provisions of SFAS 141(R) are applied prospectively, the impact cannot be determined until the transactions occur. The Company does not believe this pronouncement will have a material effect on its financial statements.

On March 20, 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133" ("SFAS 161"). SFAS 161 provides for enhanced disclosures about how and why an entity uses derivatives and how and where those derivatives and related hedged items are reported in the entity's financial statements. SFAS 161 also requires certain tabular formats for disclosing such information. SFAS 161 is effective for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. SFAS 161 applies to all entities and all derivative instruments and related hedged items accounted for under SFAS 133. Among other things, SFAS 161 requires disclosures of an entity's objectives and strategies for using derivatives by primary underlying risk and certain disclosures about the potential future collateral or cash requirements as a result of contingent credit-related features. The Company is currently evaluating the impact, if any, that the adoption of SFAS 161 will have on the Company's financial statements.

On January 12, 2009, the FASB issued FASB Staff Position ("FSP") EITF 99-20-1 "Amendments to the Impairment Guidance of EITF 99-20" ("EITF 99-20-1"), which amends the impairment guidance in EITF 99-20 to achieve more consistent determination of whether an other-than-temporary impairment has occurred for all beneficial interests within the scope of EITF 99-20. EITF 99-20-1 is effective for interim and annual reporting periods ending after December 15, 2008, on a prospective basis. EITF 99-20-1 eliminates the requirement that a holder's best estimate of cash flows be based upon those that a "market participant" would use and instead requires that an other-than-temporary impairment be recognized as a realized loss through earnings when it is "probable" there has been an adverse change in the holder's estimated cash flows from cash flows previously projected. This change is consistent with the impairment models contained in SFAS 115. EITF 99-20-1 requires that the holder consider all available information relevant to the collectability of the security, including information about past events, current conditions, and reasonable and supportable forecasts, when developing the estimate of future cash flows. Such information generally should include the remaining payment terms of the security, prepayments speeds, financial condition of the issuer, expected defaults, and the value of any underlying collateral. The holder should also consider industry analyst reports and forecasts, sector credit ratings, and other market data that are relevant to the collectability of the security. The Company's adoption of EITF 99-20-1 at December 31, 2008 did not have a material impact on the Company's financial statements.

In December 2008, the FASB issued FSP SFAS 140-4 and FIN 46(R)-8, "Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities" ("FSP SFAS 140-4" and "FIN 46(R)-8"). FSP SFAS 140-4 and FIN 46(R)-8 amends SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" ("SFAS 140") and FIN No. 46(R), "Consolidation of Variable Interest Entities (revised December 2003) – an interpretation of Accounting Research Bulletin No. 51" ("FIN 46(R)") to require additional disclosures regarding transfers of financial assets and interest in variable interest entities and is effective for interim or annual reporting periods ending after December 15, 2008. The adoption of FSP SFAS 140-4 and FIN 46(R)-8 did not have a material impact on the Company's financial statements.

In June 2008, the FASB issued FSP No. EITF 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities" ("EITF 03-6-1"). EITF 03-6-1 provides that unvested share-based

payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. The Company's adoption of EITF 03-6-1 on January 1, 2009 is not expected to have a material impact on the Company's consolidated financial statements.

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On February 20, 2008, the FASB issued FSP 140-3, “Accounting for Transfers of Financial Assets and Repurchase Financing Transactions,” (“FSP 140-3”), which provides guidance on accounting for transfers of financial assets and repurchase financings. FSP 140-3 presumes that an initial transfer of a financial asset and a repurchase financing are considered part of the same arrangement (i.e., a linked transaction) under SFAS No. 140 “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities” (“SFAS 140”). However, if certain criteria, as described in FSP 140-3, are met, the initial transfer and repurchase financing shall not be evaluated as a linked transaction and shall be evaluated separately under SFAS 140. If the linked transaction does not meet the requirements for sale accounting, the linked transaction shall generally be accounted for as a forward contract, as opposed to the current presentation, where the purchased asset and the repurchase liability are reflected separately on the balance sheet. FSP 140-3 is effective on a prospective basis for fiscal years beginning after November 15, 2008, with earlier application not permitted. The Company is currently evaluating the impact, if any, that the adoption of FSP 140-3 will have on the Company’s financial statements.

On October 10, 2008, the FASB issued FSP No. 157-3, “Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active” (“FSP 157-3”). FSP 157-3 clarifies the application of SFAS 157, “Fair Value Measurements” (“SFAS 157”) in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. The issuance of FSP 157-3 did not have any impact on the Company’s determination of fair value for its financial assets.

NOTE 3 – AGENCY MBS

The following table presents the components of the Company’s investment in Agency MBS as of December 31, 2008 and December 31, 2007:

	December 31, 2008	December 31, 2007
Principal/par value	\$ 307,548	\$ 7,400
Purchase premiums	3,585	14
Purchase discounts	(59)	(4)
Amortized cost	311,074	7,410
Gross unrealized gains	1,355	46
Gross unrealized losses	(853)	–
Fair value	\$ 311,576	\$ 7,456
Weighted average coupon	5.06%	5.43%

Principal/par value includes principal payments receivable on Agency MBS of \$956 and none as of December 31, 2008 and 2007, respectively.

The Company purchased approximately \$365,438 of Agency MBS during the year ended December 31, 2008 and financed the purchases with repurchase agreements of \$349,695. Of the Agency MBS balances at December 31, 2008 and December 31, 2007, Agency MBS with a fair value of \$300,277 and none were pledged as collateral under the repurchase agreements, respectively. The Company also sold \$29,869 of Agency MBS during the period at a net loss of \$125.

At December 31, 2008, the Company’s Agency MBS had a weighted average of 21 months to reset.

NOTE 4 – SECURITIZED MORTGAGE LOANS, NET

The following table summarizes the components of securitized mortgage loans as of December 31, 2008 and 2007.

	2008	2007
Securitized mortgage loans:		
Commercial	\$ 164,032	\$ 185,998
Single-family	70,607	86,088
	234,639	272,086
Funds held by trustees, including funds held for defeasance	11,267	7,225
Accrued interest receivable	1,538	1,940
Unamortized discounts and premiums, net	90	(67)
Loans, at amortized cost	247,534	281,184
Allowance for loan losses	(3,707)	(2,721)
	\$ 243,827	\$ 278,463

All of the securitized mortgage loans are encumbered by securitization financing bonds (see Note 9).

Commercial mortgage loans were originated principally in 1996 and 1997 and are collateralized by first deeds of trust on income producing properties. Approximately 88% of commercial mortgage loans are secured by multifamily properties and approximately 12% by office, health-care, hospital, retail, warehouse and mixed-used properties. There were two delinquent commercial mortgage loans with a total unpaid principal balance of \$3,098 as of December 31, 2008.

Single-family mortgage loans are secured by first deeds of trust on residential real estate and were originated principally from 1992 to 1997. Single-family mortgage loans includes \$167 of real estate owned, \$404 of loans in foreclosure and \$1,756 of loans more than 90 days delinquent, on which the Company continues to accrue interest.

Funds held by trustees includes \$11,118 of cash and cash equivalents held by the trust for defeased loans. These defeased funds represent replacement collateral for the defeased mortgage loan, which replicates the contractual cash flows of the defeased mortgage loan and will be used to service the debt for which the underlying mortgage on the property has been released.

NOTE 5 - ALLOWANCE FOR LOAN LOSSES

The allowance for loan losses is included in securitized mortgage loans, net in the accompanying consolidated balance sheets. The following table summarizes the aggregate activity for the allowance for loan losses for the years ended December 31, 2008, 2007 and 2006.

	2008	2007	2006
Allowance at beginning of year	\$ 2,721	\$ 4,495	\$ 19,035
Provision for (recapture of) loan losses	991	(1,281)	(15)
Credit losses, net of recoveries	(5)	(493)	(4,172)
Loans sold/transferred	–	–	(10,353)
Allowance at end of year	\$ 3,707	\$ 2,721	\$ 4,495

The following table presents certain information on impaired securitized commercial mortgage loans.

	Investment in Impaired Loans	Reserves on Impaired Loans	Investment in Excess of Reserves
2006	\$ 13,266	\$ 4,107	\$ 9,159
2007	13,792	2,590	11,202
2008	17,253	3,527	13,726

NOTE 6 – INVESTMENT IN JOINT VENTURE

The Company, through a wholly-owned subsidiary, holds a 49.875% interest in Copperhead Ventures, LLC, a joint venture primarily between the Company and DBAH Capital, LLC, an affiliate of Deutsche Bank, A.G.

The Company accounts for its investment in the joint venture using the equity method, under which it recognizes its proportionate share of the joint venture's earnings or loss and changes in accumulated other comprehensive income or loss.

The joint venture owns interests in commercial mortgage backed securities ("CMBS") and an investment in a payment agreement from the Company (see Note 10). Under the payment agreement amounts received, after payment on the associated securitization financing bonds outstanding, monthly by the Company on certain securitized commercial mortgage loans, which includes any defeased loans, are paid to the joint venture (see Note 10). During the year ended December 31, 2008, the joint venture received \$1.6 million of payments under this payment agreement.

The Company reported equity in the loss of the joint venture of \$5,733, which includes \$360 of amortization expense, and a decrease of \$3,316 in accumulated other comprehensive income of the joint venture for the year ended December 31, 2008 resulting from the venture's ownership of CMBS. The Company also recorded an adjustment to the opening balance of accumulated deficit of approximately \$380 related to the joint venture's adoption of SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"). The decline in the joint venture's equity is partially attributable to an \$8,387 distribution of excess cash received during 2008, along with the comprehensive net loss for the year.

The following table presents the condensed results of operations for the joint venture for the years ended December 31, 2008 and 2007 and the financial condition as of December 31, 2008 and 2007.

Condensed Statement of Operations	2008	2007
Interest income	\$ 3,956	\$ 5,819
Impairment	(7,278)	–
Fair value adjustments, net	(7,391)	(3,275)
General and administrative expense	(59)	–
Net (loss) income	\$ (10,772)	\$ 2,318

Condensed Balance Sheet	2008	2007
Total assets	\$ 11,240	\$ 37,972
Total liabilities	21	–
Total equity	\$ 11,219	\$ 37,972

The impairment of \$7,278 in 2008 resulted from an other-than-temporary impairment on CMBS owned by the joint venture. The net negative fair value adjustments of \$7,391 resulted from adjustments to the payment agreement discussed above. The instrument is accounted for under SFAS 159, “The Fair Value Option for Financial Assets and Financial Liabilities,” and accordingly, changes in value of this investment are recorded in the statement of operations.

NOTE 7 – OTHER INVESTMENTS

The following table summarizes the amortized cost basis and fair value of the Company's other investments and the related average effective interest rates at December 31, 2008 and 2007:

	December 31, 2008		December 31, 2007	
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield
Other securities:				
Non-Agency MBS	\$ 6,959	8.02%	\$ 7,684	6.85%
Corporate debt securities	–	–%	4,722	11.75%
Equity securities of publicly traded companies	3,441		7,704	
	10,400		20,110	
Gross unrealized gains	802		2,361	
Gross unrealized losses	(1,335)		(696)	
	9,867		21,775	
Other loans and investments	2,868		6,774	
	\$ 12,735		\$ 28,549	

The non-Agency MBS consist principally of fixed rate securities collateralized by single-family residential loans originated in 1994.

The Company sold approximately \$14,243 of equity securities during the year ended December 31, 2008, on which it recognized a gain of \$2,637, and purchased approximately \$9,988 of equity securities during 2008. The Company also sold the corporate debt security during the second quarter of 2008, on which it recognized a loss of \$187. The Company received dividends of \$1,180 and \$343 on equity securities during 2008 and 2007, respectively, which are included in "Other income (expense)" in the consolidated statement of operations. The Company recognized a net gain of \$759 and a net loss of \$207 on the sale of other investments for the years ended December 31, 2007 and 2006, respectively.

NOTE 8 – REPURCHASE AGREEMENTS

The Company uses repurchase agreements, which are recourse to the Company, to finance certain of its investments. The Company had repurchase agreements of \$274,217 at December 31, 2008, which were collateralized by Agency MBS with a fair value of \$300,277, and \$4,612 at December 31, 2007, which were collateralized by securitization financing bonds with a fair value of \$42,975.

At December 31, 2008 and December 31, 2007, the repurchase agreements had a weighted average interest rate of 2.70% and 5.07%, respectively. At December 31, 2008 and December 31, 2007, all repurchase agreements had the following original maturities:

Original Maturity	2008	2007
30 days or less	\$ 38,617	\$ 4,612
31 to 60 days	187,960	–
61 to 90 days	47,640	–
	\$ 274,217	\$ 4,612

NOTE 9 – SECURITIZATION FINANCING

The Company, through limited-purpose finance subsidiaries, has issued bonds pursuant to indentures in the form of non-recourse securitization financing. Each series of securitization financing may consist of various classes of bonds, either at fixed or variable rates of interest and having varying repayment terms. The Company, on occasion, may retain bonds or redeem bonds and hold such bonds outstanding for possible future resale or reissuance. Payments received on securitized mortgage loans and any reinvestment income earned thereon are used to make payments on the bonds.

The obligations under the securitization financings are payable solely from the securitized mortgage loans and are otherwise non-recourse to the Company. The stated maturity date for each class of bonds is generally calculated based on the final scheduled payment date of the underlying collateral pledged. The actual maturity of each class will be directly affected by the rate of principal prepayments on the related collateral. Each series is also subject to redemption at the Company's option according to specific terms of the respective indentures. As a result, the actual maturity of any class of a series of securitization financing is likely to occur earlier than its stated maturity.

The Company has three series of bonds remaining outstanding pursuant to three separate indentures. One series with a principal amount of \$28,186 is collateralized by \$70,607 in single-family mortgage loans. The two remaining series with principal amounts of \$18,256 and \$131,343, respectively, are collateralized by commercial mortgage loans with unpaid principal balances at December 31, 2008 of \$22,912 and \$141,120, respectively.

The components of securitization financing along with certain other information at December 31, 2008 and 2007 are summarized as follows:

	2008		2007	
	Bonds Outstanding	Range of Interest Rates	Bonds Outstanding	Range of Interest Rates
Fixed rate classes	\$ 149,598	6.6% - 8.8%	\$ 167,398	6.6% - 8.8%
Variable rate class	28,186	1.7%	34,500	5.1%
Accrued interest payable	1,008		1,186	
Unamortized net bond premium and deferred costs	(627)		1,301	
	\$ 178,165		\$ 204,385	
Range of stated maturities	2024-2027		2024-2027	
Estimated weighted average life	2.6 years		3.3 years	
Number of series	3		3	

At December 31, 2008, the weighted-average effective rate of the fixed rate classes was 6.9%. The variable-rate bonds pay interest based on one-month LIBOR plus 30 basis points. The average effective rate of interest for securitization financing was 6.1%, 7.2%, and 8.1%, for the years ended December 31, 2008, 2007, and 2006, respectively.

On June 15, 2008, the Company redeemed one fixed rate bond outstanding at par for \$39 as permitted by the related securitization trust's indenture. This bond had an unamortized premium of \$1,247 on the redemption date, which the Company recognized as income and reported in "Other income (expense)" in the consolidated statement of operations for the year ended December 31, 2008. The Company has the right to redeem an additional \$18,288 in bonds held at December 31, 2008 at their current unpaid principal balance.

NOTE 10 – OBLIGATION UNDER PAYMENT AGREEMENT

On January 1, 2008, the Company adopted the provisions of SFAS 159, which permits entities to choose to measure financial instruments at fair value. The Company adopted SFAS 159 to enhance the transparency of its financial condition. The effect of the adoption of SFAS 159 was to decrease beginning accumulated deficit by \$1,323. Obligation under payment agreement represents the fair value of estimated future payments due to the joint venture discussed in Note 6. The amounts due under the payment agreement are based on the amounts received monthly by the Company on certain outstanding securitized commercial mortgage loans and defeased commercial mortgage loans with an unpaid principal balance of \$152,238 at December 31, 2008, after payment of the associated securitization financing bonds outstanding with an unpaid principal balance of \$131,343 at December 31, 2008. The present value of the payment agreement was determined based on the total estimated future payments discounted at a weighted average rate of 36.5%. Factors which significantly impact the valuation of the payment agreement include the credit performance of the underlying securitized mortgage loans, estimated prepayments on the loans and the weighted average discount rate used on the cash flows.

During the year ended December 31, 2008, the Company made payments under the payment agreement of \$1,608, all of which was recorded as interest expense in the Company's financial statements.

NOTE 11 – FAIR VALUE AND ADDITIONAL INFORMATION ABOUT FINANCIAL INSTRUMENTS

On January 1, 2008, the Company adopted the provisions of SFAS 157 for all assets that are measured at fair value and for its obligation under payment agreement liability. Fair value is defined as the exchange price in an orderly transaction, that is not a forced liquidation or distressed sale, between market participants to sell an asset or transfer a liability in the market in which the reporting entity would transact for the asset or liability, that is, the principal or most advantageous market for the asset/liability. Where available, fair value is based on observable market prices or parameters or derived from such prices or parameters. Where observable prices or inputs are not available, valuation models are applied. These valuation techniques involve some level of management estimation and judgment, the degree of which is dependent on the price transparency for the instruments or market and the instruments' complexity.

Assets and liabilities recorded at fair value in the consolidated balance sheets are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Hierarchical levels, defined by SFAS 157 and directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities, are as follows:

Level 1 — Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date. The types of assets and liabilities carried at Level 1 fair value generally are equity securities listed in active markets.

Level 2 — Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the asset or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life. Fair valued assets and liabilities that are generally included in this category are Agency MBS.

Level 3 — Inputs reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model. Generally, assets and liabilities carried at fair value and included in this category are non-agency mortgage-backed securities, delinquent property tax receivables and the obligation under payment agreement liability.

The following table presents the Company's assets and liabilities at December 31, 2008, which are carried at fair value, segregated by the hierarchy level of the fair value estimate:

	Fair Value	Fair Value Measurements		
		Level 1	Level 2	Level 3
Assets:				
Agency MBS	\$ 311,576	\$ –	\$ 311,576	\$ –
Non-agency MBS	6,259	–	–	6,259
Equity securities	3,607	3,607	–	–
Other	211	–	–	211
Total assets carried at fair value	\$ 321,653	\$ 3,607	\$ 311,576	\$ 6,470
Liabilities:				
Obligation under payment agreement	\$ 8,534	\$ –	\$ –	\$ 8,534
Total liabilities carried at fair value	\$ 8,534	\$ –	\$ –	\$ 8,534

The following tables present the reconciliations of the beginning and ending balances of the Level 3 fair value estimates for the year ended December 31, 2008:

	Level 3 Fair Values				Obligation under payment agreement
	Non-Agency MBS	Corporate debt securities	Other	Total assets	
Balance at January 1, 2008	\$ 7,726	\$ 4,347	\$ 2,127	\$ 14,200	\$ (15,473)
Total realized and unrealized gains (losses) Included in the statement of operations in fair value adjustments, net	–	(187)	(9)	(195)	6,939
Included in other comprehensive income (loss)	(742)	375	15	(351)	–
Purchases, sales, issuances and other settlements, net	(725)	(4,535)	(1,922)	(7,184)	–
Transfers in and/or out of Level 3	–	–	–	–	–
Balance at December 31, 2008	\$ 6,259	\$ –	\$ 211	\$ 6,470	\$ (8,534)

There were no assets or liabilities which were measured at fair value on a non-recurring basis during the year ended December 31, 2008.

SFAS No. 107, “Disclosures about Fair Value of Financial Instruments” requires the disclosure of the estimated fair value of financial instruments. The following table presents the recorded basis and estimated fair values of the Company’s financial instruments as of December 31, 2008 and 2007:

	2008		2007	
	Recorded Basis	Fair Value	Recorded Basis	Fair Value
Assets:				
Agency MBS	\$ 311,576	\$ 311,576	\$ 7,456	\$ 7,456
Securitized mortgage loans, net	243,827	201,252	278,463	282,242
Investment in joint venture	5,655	5,595	19,267	18,847
Other investments	12,735	12,358	28,549	32,182
Liabilities:				
Repurchase agreements	274,217	274,217	4,612	4,612
Securitization financing	178,165	153,370	204,385	212,327
Obligation under payment agreement	8,534	8,534	16,796	15,473

The fair value of securitized mortgage loans and securitization financing decreased below their respective carrying values during 2008 as market volatility increased the discount rates used in calculating the fair values, which are calculated by discounting the estimated future cash flows.

NOTE 12 – EARNINGS PER SHARE

The following table reconciles the numerator and denominator for both the basic and diluted earnings per share for the years ended December 31, 2008, 2007, and 2006.

	2008		2007		2006	
	Income	Weighted Average Common Shares	Income	Weighted Average Common Shares	Income	Weighted Average Common Shares
Net income	\$ 15,121		\$ 8,899		\$ 4,909	
Preferred stock dividends	(4,010)		(4,010)		(4,044)	
Net income available to common shareholders	\$ 11,111	12,166,558	\$ 4,889	12,135,495	\$ 865	12,140,452
Net income per share:						
Basic and diluted		\$ 0.91		\$ 0.40		\$ 0.07
Net effect of dilutive stock options						
		– 3,053		– 2,593		– –
	\$ 11,111	12,169,611	\$ 4,889	12,138,088	\$ 865	12,140,452

Potentially antidilutive securities excluded from the calculation of diluted earnings per share are as follows:

	Year ended December 31,		
	2008	2007	2006
Shares issuable under stock option awards	118,053	92,407	70,000
Convertible preferred shares	4,221,539	4,221,539	4,256,237

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NOTE 13 – PREFERRED AND COMMON STOCK

The Company is authorized to issue up to 50,000,000 shares of preferred stock. For all series issued, dividends are cumulative from the date of issue and are payable quarterly in arrears. The dividends are equal, per share, to the greater of (i) the per quarter base rate of \$0.2375 for Series D, or (ii) the quarterly dividend declared on the Company's common stock. One share of Series D preferred stock is convertible at any time at the option of the holder into one share of common stock. The series is redeemable by the Company at any time, in whole or in part, (i) at a rate of one share of preferred stock for one share of common stock, plus accrued and unpaid dividends, provided that for 20 trading days within any period of 30 consecutive trading days, the closing price of the common stock equals or exceeds the issue price, or (ii) for cash at the issue price, plus any accrued and unpaid dividends.

In the event of liquidation, the holders of this series of preferred stock will be entitled to receive out of the Company's assets, prior to any such distribution to the common shareholders, the issue price per share in cash, plus any accrued and unpaid dividends. If the Company fails to pay dividends for two consecutive quarters or if the Company fails to maintain consolidated shareholders' equity of at least 200% of the aggregate issue price of the Series D preferred stock, then these shares automatically convert into a new series of 9.50% senior notes. The Company paid dividends of \$0.95 per share of Series D Preferred Stock for each of the years ended December 31, 2008, 2007 and 2006.

The following table presents the changes in the number of preferred and common shares outstanding:

	Shares	
	Preferred Series D	Common
January 1, 2006	5,628,737	12,163,391
Redeemed	(1,406,767)	-
Converted	(431)	431
Repurchased	-	(32,560)
December 31, 2006	4,221,539	12,130,831
Shares issued for stock option exercise	-	5,000
December 31, 2007	4,221,539	12,135,831
Restricted shares granted	-	33,500
December 31, 2008	4,221,539	12,169,331

In 2008, the Company issued 33,500 shares of restricted common stock in a share-based compensation award as discussed further in Note 14. The Company repurchased 32,560 shares of common stock in 2006, under a stock repurchase plan authorized by its Board of Directors in 2005. The Company has made no additional purchases since that time. Any future repurchases of common stock will be made at times and in amounts as deemed appropriate by the Company, and the plan may be suspended or discontinued at any time.

The following table presents the preferred and common dividends declared from January 1, 2008 through December 31, 2008:

Declaration Date	Record Date	Payment Date	Dividend per Share	
			Common	Preferred
Common Stock				
February 5, 2008	February 15, 2008	February 29, 2008	\$ 0.10	–
May 12, 2008	May 22, 2008	May 30, 2008	0.15	–
August 18, 2008	August 29, 2008	September 30, 2008	0.23	–
December 10, 2008	December 22, 2008	January 30, 2009	0.23	–
Preferred Stock				
March 19, 2008	March 31, 2008	April 30, 2008	– \$	0.2375
June 18, 2008	June 30, 2008	July 31, 2008	–	0.2375
September 18, 2008	September 30, 2008	October 31, 2008	–	0.2375
December 22, 2008	December 31, 2008	February 2, 2009	–	0.2375

Shelf Registration

On February 29, 2008, the Company filed a shelf registration statement on Form S-3, which became effective on April 17, 2008. The shelf registration permits the Company to sell up to \$1,000,000 of securities, including common stock, preferred stock, debt securities and warrants. No shares had been sold or otherwise issued under this shelf registration as of December 31, 2008.

NOTE 14 – EMPLOYEE BENEFITS

Stock Incentive Plan

Pursuant to the Company's 2004 Stock Incentive Plan, as approved by the shareholders at the Company's 2005 annual shareholders' meeting (the "Stock Incentive Plan"), the Company may grant to eligible officers, directors and employees stock options, stock appreciation rights ("SARs") and restricted stock awards. An aggregate of 1,500,000 shares of common stock may be granted pursuant to the Stock Incentive Plan. The Company may also grant dividend equivalent rights ("DERs") in connection with the grant of options or SARs.

On February 4, 2008, the Company granted 33,500 shares of restricted common stock to certain of its employees and officers under the Stock Incentive Plan. Of the restricted stock granted, 3,500 shares vested 25% per quarter in 2008. The remaining 30,000 shares of restricted stock vest 25% per year (on the grant date anniversary) over the next four years. The weighted average grant date fair value of the restricted stock grants was \$8.80 per share for a total compensation cost of \$294, which will be recognized evenly over the vesting period. The Company recognized expense related to the restricted stock granted of \$89 for the year ended December 31, 2008.

On May 16, 2008, the Company granted options to acquire an aggregate of 25,000 shares of common stock to its directors under the Stock Incentive Plan for which the Company recognized an expense of approximately \$13. The options granted expire on May 16, 2013 and have an exercise price of \$9.81 per share, which was 110% of the closing price of the Company's common stock on the grant date. Of the options granted, 5,000 options were issued to a new director and had a one year vesting term. The remaining options granted vested immediately. The weighted average grant-date fair value of the options granted was \$0.50 per share on the grant date.

The fair value of each SAR or option award is estimated on the date of grant using the Black-Scholes option valuation model that uses the assumptions noted in the table below. Expected volatilities are based on the historical volatility of the Company's stock and other factors. The Company uses historical data to estimate option exercise and employee termination within the valuation model. SARs are assumed to be exercised at the midpoint between the later of their vesting date and the current reporting date and the expiration date. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

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As required by SFAS 123(R), stock options, which are settleable only in shares of common stock, have been treated as equity awards, with their fair value measured at the grant date, and SARs, which are settleable in cash, have been treated as liability awards, with their fair value measured at the grant date and remeasured at the end of each reporting period.

The following table describes the weighted average of assumptions used for calculating the fair value of SARs outstanding at December 31, 2008, 2007 and 2006.

	SARs Fair Value		
	December 31,		
	2008	2007	2006
Expected volatility	21.3%-26.6%	15.0%-20.0%	17.2%-22.9%
Weighted-average volatility	24.4%	16.2%	19.4%
Expected dividends	14.1%	0%	0%
Expected term (in months)	43	49	45
Weighted-average risk-free rate	1.89%	3.5%	4.7%
Range of risk-free rates	1.73%-2.08%	3.3%-3.6%	4.7%

The following table presents a summary of the SAR activity for the year ended December 31, 2008.

	Year Ended	
	December 31, 2008	
	Number of	Weighted-
	Shares	Average
		Exercise
		Price
SARs outstanding at beginning of period	278,146	\$ 7.27
SARs granted	—	—
SARs forfeited or redeemed	—	—
SARs exercised	—	—
SARs outstanding at end of period	278,146	\$ 7.27
SARs vested and exercisable	149,860	\$ 7.41

The weighted average remaining contractual term on the SARs shares outstanding and exercisable is 43 months and 42 months, respectively.

The following table presents a summary of the option activity for the Stock Incentive Plan:

	Year Ended	
	December 31, 2008	
	Number of	Weighted-
	Shares	Average
		Exercise
		Price
Options outstanding at beginning of period	90,000	\$ 8.27
Options granted	25,000	9.81
Options forfeited or redeemed	(5,000)	9.81
Options exercised	—	—
Options outstanding at end of period	110,000	\$ 8.61

Options vested and exercisable	110,000	\$	8.61
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The Company incurred a (benefit)/expense of \$(360), \$306 and \$244 for SARs and options related to the Stock Incentive Plan during 2008, 2007 and 2006, respectively. The total compensation cost related to non-vested SAR awards was \$6 at December 31, 2008 and will be recognized as the awards vest. The weighted average period over which the total compensation cost related to the SARs at December 31, 2008 is expected to be recognized is 43 months.

Employee Savings Plan

The Company provides an Employee Savings Plan under Section 401(k) of the Code. The Employee Savings Plan allows eligible employees to defer up to 25% of their income on a pretax basis. The Company matches the employees' contribution, up to 6% of the employees' eligible compensation. The Company may also make discretionary contributions based on the profitability of the Company. The total expense related to the Company's matching and discretionary contributions in 2008, 2007, and 2006 was \$64, \$65 and \$78, respectively. The Company does not provide post employment or post retirement benefits to its employees.

NOTE 15 – COMMITMENTS AND CONTINGENCIES

As of December 31, 2008, the Company is obligated under non-cancelable operating leases with expiration dates through in December 2013. Required rental payments are as follows:

2009	\$	145
2010		149
2011		154
2012		158
2013 and thereafter		163
	\$	769

Rent and lease expense under leases which expired in previous years was \$181, \$143, and \$136, respectively in 2008, 2007, and 2006.

NOTE 16 – LITIGATION

The Company and its subsidiaries may be involved in certain litigation matters arising in the ordinary course of business. Although the ultimate outcome of these matters cannot be ascertained at this time, and the results of legal proceedings cannot be predicted with certainty, the Company believes, based on current knowledge, that the resolution of these matters arising in the ordinary course of business will not have a material adverse effect on the Company's financial position or results of operations. Information on litigation arising out of the ordinary course of business is described below.

One of the Company's subsidiaries, GLS Capital, Inc. ("GLS"), and the County of Allegheny, Pennsylvania are defendants in a class action lawsuit ("Pentlong") filed in 1997 in the Court of Common Pleas of Allegheny County, Pennsylvania (the "Court of Common Pleas"). Between 1995 and 1997, GLS purchased delinquent county property tax receivables for properties located in Allegheny County. Pentlong Plaintiffs allege that GLS did not enjoy the same rights as its assignor, Allegheny County, to recover from delinquent taxpayers certain attorney fees, costs and expenses and interest in the collection of the tax receivables. Class action status has been certified in this matter, but a motion to reconsider is pending. The Pentlong litigation was stayed pending the outcome of similar litigation before the Pennsylvania Supreme Court in a case in which GLS was not a defendant. The plaintiff in that case had disputed

the application of curative legislation enacted in 2003 but retroactive to 1996 which specifically set forth the right to collect reasonable attorney fees, costs, and interest which were properly taxable as part of the tax debt owed. The Pennsylvania Supreme Court subsequently issued an opinion in favor of the defendants in that matter, which the Company believes will favorably impact the Pentlong litigation by substantially reducing Pentlong Plaintiffs' universe of actionable claims against GLS in connection with the collection of the tax receivables. No timetable has been set by the Court of Common Pleas for the recommencement of the litigation. Pentlong Plaintiffs have not enumerated their damages in this matter.

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Dynex Capital, Inc. and Dynex Commercial, Inc. (“DCI”), a former affiliate of the Company and now known as DCI Commercial, Inc., are appellees (or respondents) in the Supreme Court of Texas related to the matter of Basic Capital Management, Inc. et al. (collectively, “BCM” or the “Plaintiffs”) versus DCI et al. The appeal seeks to overturn the trial court’s judgment, and subsequent affirmation by the Fifth Court of Appeals at Dallas, in the Company’s and DCI’s favor which denied recovery to Plaintiffs. Plaintiffs are seeking reversal of the trial court’s judgment and sought rendition of judgment against the Company for alleged breach of loan agreements for tenant improvements in the amount of \$253.

They also seek reversal of the trial court’s judgment and rendition of judgment against DCI in favor of BCM under two mutually exclusive damage models, for \$2,200 and \$25,600, respectively, related to the alleged breach by DCI of a \$160,000 “master” loan commitment. Plaintiffs also seek reversal and rendition of a judgment in their favor for attorneys’ fees in the amount of \$2,100. Alternatively, Plaintiffs seek a new trial. Even if Plaintiffs were to be successful on appeal, DCI is a former affiliate of the Company, and the Company believes that it would have no obligation for amounts, if any, awarded to the Plaintiffs as a result of the actions of DCI.

Dynex Capital, Inc. and MERIT Securities Corporation, a subsidiary, were defendants in a putative class action complaint alleging violations of the federal securities laws in the United States District Court for the Southern District of New York (“District Court”) by the Teamsters Local 445 Freight Division Pension Fund (“Teamsters”). The complaint was filed on February 7, 2005, and purported to be a class action on behalf of purchasers between February 2000 and May 2004 of MERIT Series 12 and MERIT Series 13 securitization financing bonds, which are collateralized by manufactured housing loans. After a series of rulings by the District Court and an appeal by the Company and MERIT, on February 22, 2008, the United States Court of Appeals for the Second Circuit dismissed the litigation against the Company and MERIT. Teamsters filed an amended complaint on August 6, 2008 with the District Court which essentially restated the same allegations as the original complaint and added the Company’s former president and its current Chief Operating Officer as defendants. The Company is seeking to have the amended complaint dismissed and intends to vigorously defend itself in this matter.

Although no assurance can be given with respect to the ultimate outcome of the above litigation, the Company believes the resolution of these lawsuits will not have a material effect on its consolidated balance sheet but could materially affect its consolidated results of operations in a given year or period.

NOTE 17 – SUPPLEMENTAL CONSOLIDATED STATEMENTS OF CASH FLOWS INFORMATION

	Years ended December 31,		
	2008	2007	2006
Cash paid for interest	\$ 19,817	\$ 20,082	\$ 40,932
Supplemental disclosure of non-cash activities:			
Formation of joint venture with Deutsche Bank	\$ –	\$ –	\$ 38,248
Conversion of preferred shares to common shares	\$ –	\$ –	\$ 4

NOTE 18 – RELATED PARTY TRANSACTIONS

As discussed in Note 16, the Company and DCI have been jointly named in litigation regarding the activities of DCI while it was an operating subsidiary of an affiliate of the Company. The Company and DCI entered into a Litigation Cost Sharing Agreement whereby the parties set forth how the costs of defending against litigation would be shared, and whereby the Company agreed to fund all costs of such litigation, including DCI’s portion. DCI’s cumulative portion of costs associated with litigation and funded by the Company is \$3,299 and is secured by the proceeds of any counterclaims that DCI may receive in the litigation. DCI costs funded by the Company are loans and bear simple interest at the rate of Prime plus 8.0% per annum. At December 31, 2008, the total amount due the Company under

the Litigation Cost Sharing Agreement, including interest, was \$6,102, which has been fully reserved by the Company. DCI is currently wholly owned by ICD Holding, Inc. An executive of the Company is the sole shareholder of ICD Holding.

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NOTE 19 – NON-CONSOLIDATED AFFILIATES

The Company holds a 1% limited partnership interest in a partnership that owns a low-income housing tax credit multifamily housing property located in Texas. The Company has loaned the partnership \$931, \$50 of which was advanced to the partnership during 2008. These advances and the accrued interest thereon are due on demand. The Company, through a subsidiary, has made a first mortgage loan to the partnership secured by the property, with a current unpaid principal balance of \$1,464. Because the Company does not have control or exercise significant influence over the operations of this partnership, its investment in the partnership is accounted for using the cost method.

NOTE 20 – SUMMARY OF QUARTERLY RESULTS (UNAUDITED)

The following tables present the Company's unaudited selected quarterly results for 2008 and 2007.

Year Ended December 31, 2008	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Operating results:				
Net interest income	\$ 2,421	\$ 2,501	\$ 2,787	\$ 2,838
Net interest income after provision for loan losses	2,395	2,180	2,338	2,643
Net income	5,319	4,296	3,045	2,461
Basic net income per common share	0.36	0.27	0.17	0.12
Diluted net income per common share	0.32	0.26	0.17	0.12
Cash dividends declared per common share	0.10	0.15	0.23	0.23

Year Ended December 31, 2007	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Operating results:				
Net interest income	\$ 2,460	\$ 2,963	\$ 2,457	\$ 2,803
Net interest income after provision for loan losses	2,983	3,665	2,584	2,732
Net income	1,942	2,702	2,686	1,569
Basic and diluted net income per common share	0.08	0.14	0.14	0.05
Cash dividends declared per common share	–	–	–	–