

FIRST BANCORP /PR/
Form 10-K
March 02, 2010

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K**

(Mark one)

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES
EXCHANGE ACT OF 1934
For the Fiscal Year Ended December 31, 2009**

**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 No.)

1519 Ponce de León Avenue, Stop 23

Santurce, Puerto Rico

(Address of principal executive office)

00908

(Zip Code)

Registrant's telephone number, including area code:

(787) 729-8200

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

Title of Each Class

Name of Each Exchange on Which Registered

**Common Stock (\$1.00 par value)
7.125% Noncumulative Perpetual Monthly Income
Preferred Stock, Series A (Liquidation Preference
\$25 per share)
8.35% Noncumulative Perpetual Monthly Income
Preferred Stock, Series B (Liquidation Preference
\$25 per share)
7.40% Noncumulative Perpetual Monthly Income
Preferred Stock, Series C (Liquidation Preference
\$25 per share)
7.25% Noncumulative Perpetual Monthly Income
Preferred Stock, Series D (Liquidation Preference
\$25 per share)
7.00% Noncumulative Perpetual Monthly Income
Preferred Stock, Series E (Liquidation Preference
\$25 per share)**

**New York Stock Exchange
New York Stock Exchange

New York Stock Exchange

New York Stock Exchange

New York Stock Exchange

New York Stock Exchange**

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

NONE

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

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

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

Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate Website, 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definite proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.
Indicate by check mark whether the 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 Act). Yes No

The aggregate market value of the voting common equity held by non affiliates of the registrant as of June 30, 2009 (the last day of the registrant's most recently completed second quarter) was \$328,696,232 based on the closing price of \$3.95 per share of common stock on the New York Stock Exchange on June 30, 2009. The registrant had no nonvoting common equity outstanding as of June 30, 2009. For the purposes of the foregoing calculation only, registrant has treated as common stock held by affiliates only common stock of the registrant held by its directors and executive officers and voting stock held by the registrant's employee benefit plans. The registrant's response to this item is not intended to be an admission that any person is an affiliate of the registrant for any purposes other than this response.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date: 92,542,722 shares as of January 31, 2010.

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DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Proxy Statement for the Annual Meeting of Stockholders to be held in April 2010, which will be filed with the Securities and Exchange Commission within 120 days after the end of the registrant's fiscal year ended December 31, 2009, are incorporated by reference into Part III, Items 10, 11, 12, 13 and 14, of this Form-10-K.

FIRST BANCORP
2009 ANNUAL REPORT ON FORM 10-K
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Forward Looking Statements

This Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. When used in this Form 10-K 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's actions to improve its capital structure will have their intended effect;

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

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, including the value of derivative instruments used for protection from interest rate fluctuations;

the Corporation's reliance on brokered certificates of deposit and its ability to continue to rely on the issuance of brokered certificates of deposit to fund operations and provide liquidity;

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;

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

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 System (the Federal Reserve), the Federal Deposit Insurance Corporation (FDIC), government-sponsored housing agencies and local regulators in Puerto Rico and the U.S. and British

Virgin Islands;

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;

risks of an additional allowance as a result of an analysis of the ability to generate sufficient income to

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realize the benefit of the deferred tax asset;

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

changes in the Corporation's expenses associated with acquisitions and dispositions;

developments in technology;

the impact of Doral Financial Corporation's financial condition on the repayment of its outstanding secured loans to the Corporation;

risks associated with further downgrades in the credit ratings of the Corporation's securities;

general competitive factors and industry consolidation; and

the possible future dilution to holders of our 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 carefully consider these factors and the risk factors outlined under Item 1A, Risk Factors, in this Annual Report on Form 10-K.

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PART I

FirstBanCorp, incorporated under the laws of the Commonwealth of Puerto Rico, is sometimes referred to in this Annual Report on Form 10-K as the Corporation, we, our, the Registrant.

Item 1. Business

GENERAL

First BanCorp is a publicly-owned financial holding company that is subject to regulation, supervision and examination by the Federal Reserve Board (the FED). The Corporation was incorporated under the laws of the Commonwealth of Puerto Rico to serve as the bank holding company for FirstBank Puerto Rico (FirstBank or the Bank). The Corporation is a full service provider of financial services and products with operations in Puerto Rico, the United States and the US and British Virgin Islands. As of December 31, 2009, the Corporation had total assets of \$19.6 billion, total deposits of \$12.7 billion and total stockholders equity of \$1.6 billion.

The Corporation provides a wide range of financial services for retail, commercial and institutional clients. As of December 31, 2009, the Corporation controlled three wholly-owned subsidiaries: FirstBank, FirstBank Insurance Agency, Inc. (FirstBank Insurance Agency) and Grupo Empresas de Servicios Financieros (d/b/a PR Finance Group). FirstBank is a Puerto Rico-chartered commercial bank, FirstBank Insurance Agency is a Puerto Rico-chartered insurance agency and PR Finance Group is a domestic corporation.

FirstBank is subject to the supervision, examination and regulation of both the Office of the Commissioner of Financial Institutions of the Commonwealth of Puerto Rico (OCIF) and the Federal Deposit Insurance Corporation (the FDIC). Deposits are insured through the FDIC Deposit Insurance Fund. In addition, within FirstBank, the Bank's United States Virgin Islands operations are subject to regulation and examination by the United States Virgin Islands Banking Board, and the British Virgin Islands operations are subject to regulation by the British Virgin Islands Financial Services Commission. FirstBank Insurance Agency is subject to the supervision, examination and regulation of the Office of the Insurance Commissioner of the Commonwealth of Puerto Rico and operates nine offices in Puerto Rico. PR Finance Group is subject to the supervision, examination and regulation of the OCIF.

FirstBank conducted its business through its main office located in San Juan, Puerto Rico, forty-eight full service banking branches in Puerto Rico, sixteen branches in the United States Virgin Islands (USVI) and British Virgin Islands (BVI) and ten branches in the state of Florida (USA). FirstBank had six wholly-owned subsidiaries with operations in Puerto Rico: First Leasing and Rental Corporation, a vehicle leasing company with two offices in Puerto Rico; First Federal Finance Corp. (d/b/a Money Express La Financiera), a finance company specializing in the origination of small loans with twenty-seven offices in Puerto Rico; First Mortgage, Inc. (First Mortgage), a residential mortgage loan origination company with thirty-eight offices in FirstBank branches and at stand alone sites; First Management of Puerto Rico, a domestic corporation; FirstBank Puerto Rico Securities Corp, a broker-dealer subsidiary created in March 2009 and engaged in municipal bond underwriting and financial advisory services on structured financings principally provided to government entities in the Commonwealth of Puerto Rico; and FirstBank Overseas Corporation, an international banking entity organized under the International Banking Entity Act of Puerto Rico. FirstBank had three subsidiaries with operations outside of Puerto Rico: First Insurance Agency VI, Inc., an insurance agency with three offices that sells insurance products in the USVI; and First Express, a finance company specializing in the origination of small loans with three offices in the USVI.

Effective July 1, 2009, the Corporation consolidated the operations of FirstBank Florida, formerly a stock savings and loan association indirectly owned by the Corporation, with and into FirstBank Puerto Rico and dissolved Ponce General Corporation, former holding company of FirstBank Florida. On October 30, 2009, the Corporation divested its motor vehicle rental operations held through First Leasing and Rental Corporation through the sale of such business.

Table of Contents**BUSINESS SEGMENTS**

The Corporation has six reportable segments: Commercial and Corporate Banking; Mortgage Banking; Consumer (Retail) Banking; Treasury and Investments; United States Operations; and Virgin Islands Operations. These segments are described below:

Commercial and Corporate Banking

The Commercial and Corporate Banking segment consists of the Corporation's lending and other services for the public sector and specialized industries such as healthcare, tourism, financial institutions, food and beverage, shopping centers and middle-market clients. The Commercial and Corporate Banking segment offers commercial loans, including commercial real estate and construction loans, and other products such as cash management and business management services. A substantial portion of this portfolio is secured by the underlying value of the real estate collateral, and collateral and the personal guarantees of the borrowers are taken in abundance of caution. Although commercial loans involve greater credit risk than a typical residential mortgage loan because they are larger in size and more risk is concentrated in a single borrower, the Corporation has and maintains a credit risk management infrastructure designed to mitigate potential losses associated with commercial lending, including strong underwriting and loan review functions, sales of loan participations and continuous monitoring of concentrations within portfolios.

Mortgage Banking

The Mortgage Banking segment conducts its operations mainly through FirstBank and its mortgage origination subsidiary, FirstMortgage. These operations consist of the origination, sale and servicing of a variety of residential mortgage loans products. Originations are sourced through different channels such as branches, mortgage bankers and real estate brokers, and in association with new project developers. FirstMortgage focuses on originating residential real estate loans, some of which conform to Federal Housing Administration (FHA), Veterans Administration (VA) and Rural Development (RD) standards. Loans originated that meet FHA standards qualify for the federal agency's insurance program whereas loans that meet VA and RD standards are guaranteed by their respective federal agencies. In December 2008, the Corporation obtained from the Government National Mortgage Association (GNMA) the necessary Commitment Authority to issue GNMA mortgage-backed securities. Under this program, during 2009, the Corporation completed the securitization of approximately \$305.4 million of FHA/VA mortgage loans into GNMA MBS.

Mortgage loans that do not qualify under these programs are commonly referred to as conventional loans. Conventional real estate loans could be conforming and non-conforming. Conforming loans are residential real estate loans that meet the standards for sale under the Fannie Mae (FNMA) and Freddie Mac (FHLMC) programs whereas loans that do not meet the standards are referred to as non-conforming residential real estate loans. The Corporation's strategy is to penetrate markets by providing customers with a variety of high quality mortgage products to serve their financial needs faster and simpler and at competitive prices. The Mortgage Banking segment also acquires and sells mortgages in the secondary markets. Residential real estate conforming loans are sold to investors like FNMA and FHLMC. More than 90% of the Corporation's residential mortgage loan portfolio consists of fixed-rate, fully amortizing, full documentation loans that have a lower risk than the typical sub-prime loans that have adversely affected the U.S. real estate market. The Corporation is not active in negative amortization loans or option adjustable rate mortgage loans (ARMs) including ARMs with teaser rates.

Consumer (Retail) Banking

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 in Puerto Rico. Loans to consumers include auto, boat, lines of credit, and personal loans. Deposit products include interest bearing and non-interest bearing checking and savings accounts, Individual Retirement Accounts (IRA) and retail certificates of deposit. Retail deposits gathered through each branch of FirstBank's retail network serve as one of the funding sources for the lending and investment activities.

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Consumer lending has been mainly driven by auto loan originations. The Corporation follows a strategy of seeking to provide outstanding service to selected auto dealers that provide the channel for the bulk of the Corporation's auto loan originations. This strategy is directly linked to our commercial lending activities as the Corporation maintains strong and stable auto floor plan relationships, which are the foundation of a successful auto loan generation operation. The Corporation's commercial relations with floor plan dealers are strong and directly benefit the Corporation's consumer lending operation and are managed as part of the consumer banking activities.

Personal loans and, to a lesser extent, marine financing and a small revolving credit portfolio also contribute to interest income generated on consumer lending. Credit card accounts are issued under the Bank's name through an alliance with FIA Card Services (Bank of America), which bears the credit risk. Management plans to continue to be active in the consumer loans market, applying the Corporation's strict underwriting standards.

Treasury and Investments

The Treasury and Investments segment is responsible for the Corporation's treasury and investment management functions. In the treasury function, which includes funding and liquidity management, this segment sells funds to the Commercial and Corporate Banking, Mortgage Banking, and Consumer (Retail) Banking segments to finance their lending activities and purchases funds gathered by those segments. Funds not gathered by the different business units are obtained by the Treasury Division through wholesale channels, such as brokered deposits, Advances from the FHLB and repurchase agreements with investment securities, among others.

Since the Corporation is a net borrower of funds, the securities portfolio does not result from the investment of excess funds. The securities portfolio is a leverage strategy for the purposes of liquidity management, interest rate management and earnings enhancement.

The interest rates charged or credited by Treasury and Investments are based on market rates.

United States Operations

The United States operations segment consists of all banking activities conducted by FirstBank in the United States mainland. The Corporation provides a wide range of banking services to individual and corporate customers in the state of Florida through its ten branches and two specialized lending centers. In the United States, the Corporation originally had an agency lending office in Miami, Florida. Then, it acquired Coral Gables-based Ponce General (the parent company of Unibank, a savings and loans bank in 2005) and changed the savings and loan's name to FirstBank Florida. Those two entities were operated separately. In 2009, the Corporation filed an application with the Office of Thrift Supervision to surrender the Miami-based FirstBank Florida charter and merge its assets into FirstBank Puerto Rico, the main subsidiary of First BanCorp. The Corporation placed the entire Florida operation under the control of a new appointed Executive Vice President. The merger allows the Florida operations to benefit by leveraging the capital position of FirstBank Puerto Rico and thereby provide them with the support necessary to grow in the Florida market.

Virgin Islands Operations

The Virgin Islands operations segment consists of all banking activities conducted by FirstBank in the U.S. and British Virgin Islands, including retail and commercial banking services. In 2002, after acquiring Chase Manhattan Bank operations in the Virgin Islands, FirstBank became the largest bank in the Virgin Islands (USVI & BVI), serving St. Thomas, St. Croix, St. John, Tortola and Virgin Gorda, with 16 branches. In 2008, FirstBank acquired the Virgin Island Community Bank (VICB) in St. Croix, increasing its customer base and share in this market. The Virgin Islands operations segment is driven by its consumer and commercial lending and deposit-taking activities. Loans to consumers include auto, boat, lines of credit, personal loans and residential mortgage loans. Deposit products include interest bearing and non-interest bearing checking and savings accounts, Individual Retirement Accounts (IRA) and retail certificates of deposit. Retail deposits gathered through each branch serve as the funding sources for the lending activities.

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For information regarding First BanCorp's reportable segments, please refer to Note 33, Segment Information, to the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K.

Employees

As of December 31, 2009, the Corporation and its subsidiaries employed 2,713 persons. None of its employees are represented by a collective bargaining group. The Corporation considers its employee relations to be good.

SIGNIFICANT EVENTS DURING 2009***Participation in the U.S. Treasury Department's Capital Purchase Program***

On January 16, 2009, the Corporation entered into a Letter Agreement with the United States Department of the Treasury (Treasury) pursuant to which Treasury invested \$400,000,000 in preferred stock of the Corporation under the Treasury's Troubled Asset Relief Program Capital Purchase Program. Under the Letter Agreement, which incorporates the Securities Purchase Agreement Standard Terms (the Purchase Agreement), the Corporation issued and sold to Treasury (1) 400,000 shares of the Corporation's Fixed Rate Cumulative Perpetual Preferred Stock, Series F, \$1,000 liquidation preference per share (the Series F Preferred Stock), and (2) a warrant dated January 16, 2009 (the Warrant) to purchase 5,842,259 shares of the Corporation's common stock (the Warrant shares) at an exercise price of \$10.27 per share. The exercise price of the Warrant was determined based upon the average of the closing prices of the Corporation's common stock during the 20-trading day period ended December 19, 2008, the last trading day prior to the date the Corporation's application to participate in the program was preliminarily approved. The Purchase Agreement is incorporated into Exhibit 10.4 hereto by reference to Exhibit 10.1 of the Corporation's Form 8-K filed with the SEC on January 20, 2009.

The Series F Preferred Stock qualifies as Tier 1 regulatory capital. Cumulative dividends on the Series F Preferred Stock will accrue on the liquidation preference amount 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 F Preferred Stock will rank pari passu with the Corporation's existing 7.125% Noncumulative Perpetual Monthly Income Preferred Stock, Series A, 8.35% Noncumulative Perpetual Monthly Income Preferred Stock, Series B, 7.40% Noncumulative Perpetual Monthly Income Preferred Stock, Series C, 7.25% Noncumulative Perpetual Monthly Income Preferred Stock, Series D, and 7.00% Noncumulative Perpetual Monthly Income Preferred Stock, Series E, in terms of dividend payments and distributions upon liquidation, dissolution and winding up of the Corporation. The Purchase Agreement contains limitations on 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), of common stock prior to October 14, 2008, which is \$0.07 per share. The ability of the Corporation to purchase, redeem or otherwise acquire for consideration, any shares of its common stock, preferred stock or trust preferred securities are subject to restrictions outlined in the Purchase Agreement, including upon a default in the payment of dividends. The Corporation suspended the payment of dividends effective in August 2009. These restrictions will terminate on the earlier of (a) January 16, 2012 and (b) the date on which the Series F Preferred Stock is redeemed in whole or Treasury transfers all of the Series F Preferred Stock to third parties that are not affiliates of Treasury.

The shares of Series F Preferred Stock are non-voting, other than having class voting rights on certain matters that could adversely affect the Series F Preferred Stock. If dividends on the Series F Preferred Stock have not been paid for an aggregate of six quarterly dividend periods or more, whether or not consecutive, the Corporation's authorized number of directors will be increased automatically by two and the holders of the Series F Preferred Stock, voting together with holders of any then outstanding parity stock, will have the right to elect two directors to fill such newly created directorships at the Corporation's next annual meeting of stockholders or at a special meeting of stockholders called for that purpose prior to such annual meeting. These preferred share directors will be elected annually and will serve until all accrued and unpaid dividends on the Series F Preferred Stock have been declared and paid in full.

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On January 13, 2009, the Corporation filed a Certificate of Designations (the Certificate of Designations) with the Puerto Rico Department of State for the purpose of amending its Certificate of Incorporation to fix the designations, preferences, limitations and relative rights of the Series F Preferred Stock.

As per the Purchase Agreement, prior to January 16, 2012, the Corporation may redeem, subject to the approval of the Board of Governors of the Federal Reserve System, the shares of Series F Preferred Stock only with proceeds from one or more Qualified Equity Offerings, as such term is defined in the Certificate of Designations. After January 16, 2012, the Corporation may redeem, subject to the approval of the Board of Governors of the Federal Reserve System, in whole or in part, out of funds legally available therefore, the shares of Series F Preferred Stock then outstanding. Pursuant to the American Recovery and Reinvestment Act of 2009, subject to consultation with the appropriate Federal banking agency, the Secretary of Treasury may permit a TARP recipient to repay any financial assistance previously provided under TARP without regard to whether the financial institution has replaced such funds from any other source.

The Warrant has a ten-year term and is exercisable at any time for 5,842,259 shares of First BanCorp common stock at an exercise price of \$10.27. The exercise price and the number of shares of common stock issuable upon exercise of the Warrant are adjustable in a number of circumstances, as discussed below. The exercise price and the number of shares of common stock issuable upon exercise of the Warrant will be adjusted proportionately:

in the event of a stock split, subdivision, reclassification or combination of the outstanding shares of common stock;

until the earlier of the date the Treasury no longer holds the Warrant or any portion thereof or January 16, 2012, if the Corporation issues shares of common stock or securities convertible into common stock for no consideration or at a price per share that is less than 90% of the market price on the last trading day preceding the date of the pricing of such sale. Any amounts that the Corporation receives in connection with the issuance of such shares or convertible securities will be deemed to be equal to the sum of the net offering price of all such securities plus the minimum aggregate amount, if any, payable upon exercise or conversion of any such convertible securities; no adjustment will be required with respect to (i) consideration for or to fund business or asset acquisitions, (ii) shares issued in connection with employee benefit plans and compensation arrangements in the ordinary course consistent with past practice approved by the Corporation's Board of Directors, (iii) a public or broadly marketed offering and sale by the Corporation or its affiliates of the Corporation's common stock or convertible securities for cash pursuant to registration under the Securities Act or issuance under Rule 144A on a basis consistent with capital raising transactions by comparable financial institutions, and (iv) the exercise of preemptive rights on terms existing on January 16, 2009;

in connection with the Corporation's distributions to security holders (e.g., stock dividends);

in connection with certain repurchases of common stock by the Corporation; and

in connection with certain business combinations.

None of the shares of Series F Preferred Stock, the Warrant, or the Warrant shares are subject to any contractual restriction on transfer. The Series F Preferred Stock and the Warrant were issued in a private placement exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended. The Corporation registered for resale shares of Series F Preferred Stock, the Warrant and the Warrant shares, and the sale of the Warrant shares by the Corporation to any purchasers of the Warrant. In addition, under the shelf registration, the Corporation registered the resale of 9,250,450 shares of common stock by or on behalf of the Bank of Nova Scotia, its pledges, donees, transferees or other successors in interest.

Under the terms of the Purchase Agreement, (i) the Corporation amended its compensation, bonus, incentive and other benefit plans, arrangements and agreements (including severance and employment agreements), to the extent necessary to be in compliance with the executive compensation and corporate governance requirements of Section 111(b) of the Emergency Economic Stability Act of 2008 and applicable guidance or regulations and (ii) each Senior

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Executive Officer, as defined in the Purchase Agreement, executed a written waiver releasing Treasury and the Corporation from any claims that such officers may otherwise have as a result of the Corporation's amendment of such arrangements and agreements to be in compliance with Section 111(b). Until such time as Treasury ceases to own any debt or equity securities of the Corporation acquired pursuant to the Purchase Agreement, the Corporation must maintain compliance with these requirements.

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Reduction of credit exposure with financial institutions

The Corporation has continued working on the reduction of its credit exposure with Doral and R&G Financial. During the second quarter of 2009, the Bank purchased from R&G Financial \$205 million of residential mortgages that previously served as collateral for a commercial loan extended to R&G . The purchase price of the transaction was retained by the Corporation to fully pay off the commercial loan, thereby significantly reducing the Corporation s exposure to a single borrower. As of December 31, 2009, there still an outstanding balance of \$321.5 million due from Doral.

Surrender of the stock savings and loans association charter in Florida

Effective July 1, 2009 as part of the merger of FirstBank Florida with and into FirstBank Puerto Rico, FirstBank Florida surrendered its stock savings and loans association charter granted by the Office of Thrift Supervision. Under the regulatory oversight of the Federal Deposit Insurance Corporation and under the FirstBank Florida trade name, FirstBank continues to offer the same services offered by the former stock savings and loans association through its branch network in Florida.

Dividend Suspension

On July 30, 2009, after reporting a net loss for the quarter ended June 30, 2009, the Corporation announced that the Board of Directors resolved to suspend the payment of the common and preferred dividends, including the Series F Preferred Stock, effective with the preferred dividend payments for the month of August 2009.

Business Developments

Effective July 1, 2009, the Corporation consolidated the operations of FirstBank Florida, formerly a stock savings and loan association indirectly owned by the Corporation, with and into FirstBank Puerto Rico and dissolved Ponce General Corporation, former holding company of FirstBank Florida. On October 31, 2009, First Leasing and Rental Corporation sold its motor vehicle rental operations and realized a nominal gain of \$0.2 million.

Credit Ratings

The Corporation s credit as long-term issuer is currently rated B by Standard & Poor s (S&P) and B- by Fitch Ratings Limited (Fitch); both with negative outlook.

FirstBank s long-term senior debt rating is currently rated B1 by Moody s Investor Service (Moodys), four notches below their definition of investment grade; B by S&P, and B by Fitch, both five notches under their definition of investment grade. The outlook on the Bank s credit ratings from the three rating agencies is negative.

WEBSITE ACCESS TO REPORT

The Corporation makes available annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports, filed or furnished pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934, free of charge on or through its internet website at www.firstbankpr.com, (under the Investor Relations section), as soon as reasonably practicable after the Corporation electronically files such material with, or furnishes it to, the SEC.

The Corporation also makes available the Corporation s corporate governance guidelines, the charters of the audit, asset/liability, compensation and benefits, credit, strategic planning, corporate governance and nominating committees and the codes and principles mentioned below, free of charge on or through its internet website at www.firstbankpr.com (under the Investor Relations section):

Code of Ethics for Senior Financial Officers

Code of Ethics applicable to all employees

Independence Principles for Directors

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The corporate governance guidelines, and the aforementioned charters and codes may also be obtained free of charge by sending a written request to Mr. Lawrence Odell, Executive Vice President and General Counsel, PO Box 9146, San Juan, Puerto Rico 00908.

The public may read and copy any materials First BanCorp files with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. In addition, the public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site that contains reports, proxy, and information statements, and other information regarding issuers that file electronically with the SEC at its website (www.sec.gov).

MARKET AREA AND COMPETITION

Puerto Rico, where the banking market is highly competitive, is the main geographic service area of the Corporation. As of December 31, 2009, the Corporation also had a presence in the state of Florida and in the United States and British Virgin Islands. Puerto Rico banks are subject to the same federal laws, regulations and supervision that apply to similar institutions in the United States mainland.

Competitors include other banks, insurance companies, mortgage banking companies, small loan companies, automobile financing companies, leasing companies, brokerage firms with retail operations, and credit unions in Puerto Rico, the Virgin Islands and the state of Florida. The Corporation's businesses compete with these other firms with respect to the range of products and services offered and the types of clients, customers, and industries served.

The Corporation's ability to compete effectively depends on the relative performance of its products, the degree to which the features of its products appeal to customers, and the extent to which the Corporation meets clients' needs and expectations. The Corporation's ability to compete also depends on its ability to attract and retain professional and other personnel, and on its reputation.

The Corporation encounters intense competition in attracting and retaining deposits and its consumer and commercial lending activities. The Corporation competes for loans with other financial institutions, some of which are larger and have greater resources available than those of the Corporation. Management believes that the Corporation has been able to compete effectively for deposits and loans by offering a variety of transaction account products and loans with competitive features, by pricing its products at competitive interest rates, by offering convenient branch locations, and by emphasizing the quality of its service. The Corporation's ability to originate loans depends primarily on the rates and fees charged and the service it provides to its borrowers in making prompt credit decisions. There can be no assurance that in the future the Corporation will be able to continue to increase its deposit base or originate loans in the manner or on the terms on which it has done so in the past.

SUPERVISION AND REGULATION

Recent Events affecting the Corporation

Events since early 2008 affecting the financial services industry and, more generally, the financial markets and the economy as a whole, have led to various proposals for changes in the regulation of the financial services industry. In 2009, the House of Representatives passed the Wall Street Reform and Consumer Protection Act of 2009, which, among other things, calls for the establishment of a Consumer Financial Protection Agency having broad authority to regulate providers of credit, savings, payment and other consumer financial products and services; creates a new structure for resolving troubled or failed financial institutions; requires certain over-the-counter derivative transactions to be cleared in a central clearinghouse and/or effected on the exchange; revises the assessment base for the calculation of the Federal Deposit Insurance Corporation (FDIC) assessments; and creates a structure to regulate systemically important financial companies, including providing regulators with the power to require such companies to sell or transfer assets and terminate activities if they determine that the size or scope of activities of the company pose a threat to the safety and soundness of the company or the financial stability of the United States. Other proposals have been made, including additional capital and liquidity requirements and limitations on size or types of activity in which banks may engage. It is not clear at this time which of these proposals will be finally

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enacted into law, or what form they will take, or what new proposals may be made, as the debate over financial reform continues in 2010. The description below summarizes the current regulatory structure in which the Corporation operates. In the event the regulatory structure change significantly, the structure of the Corporation and the products and services it offers could also change significantly as a result.

Bank Holding Company Activities and Other Limitations

The Corporation is subject to ongoing regulation, supervision, and examination by the Federal Reserve Board, and is required to file with the Federal Reserve Board periodic and annual reports and other information concerning its own business operations and those of its subsidiaries. In addition, the Corporation is subject to regulation under the Bank Holding Company Act of 1956, as amended (Bank Holding Company Act). Under the provisions of the Bank Holding Company Act, a bank holding company must obtain Federal Reserve Board approval before it acquires direct or indirect ownership or control of more than 5% of the voting shares of another bank, or merges or consolidates with another bank holding company. The Federal Reserve Board also has authority under certain circumstances to issue cease and desist orders against bank holding companies and their non-bank subsidiaries.

A bank holding company is prohibited under the Bank Holding Company Act, with limited exceptions, from engaging, directly or indirectly, in any business unrelated to the businesses of banking or managing or controlling banks. One of the exceptions to these prohibitions permits ownership by a bank holding company of the shares of any corporation if the Federal Reserve Board, after due notice and opportunity for hearing, by regulation or order has determined that the activities of the corporation in question are so closely related to the businesses of banking or managing or controlling banks as to be a proper incident thereto.

Under the Federal Reserve Board policy, a bank holding company such as the Corporation is expected to act as a source of financial strength to its banking subsidiaries and to commit support to them. This support may be required at times when, absent such policy, the bank holding company might not otherwise provide such support. In the event of a bank holding company's bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain capital of a subsidiary bank will be assumed by the bankruptcy trustee and be entitled to a priority of payment. In addition, any capital loans by a bank holding company to any of its subsidiary banks must be subordinated in right of payment to deposits and to certain other indebtedness of such subsidiary bank. As of December 31, 2009, FirstBank was the only depository institution subsidiary of the Corporation.

The Gramm-Leach-Bliley Act (the GLB Act) revised and expanded the provisions of the Bank Holding Company Act by including a section that permits a bank holding company to elect to become a financial holding company and engage in a full range of financial activities. In April 2000, the Corporation filed an election with the Federal Reserve Board and became a financial holding company under the GLB Act. The GLB Act requires a bank holding company that elects to become a financial holding company to file a written declaration with the appropriate Federal Reserve Bank and comply with the following (and such compliance must continue while the entity is treated as a financial holding company): (i) state that the bank holding company elects to become a financial holding company; (ii) provide the name and head office address of the bank holding company and each depository institution controlled by the bank holding company; (iii) certify that all depository institutions controlled by the bank holding company are well-capitalized as of the date the bank holding company files for the election; (iv) provide the capital ratios for all relevant capital measures as of the close of the previous quarter for each depository institution controlled by the bank holding company; and (v) certify that all depository institutions controlled by the bank holding company are well-managed as of the date the bank holding company files the election. All insured depository institutions controlled by the bank holding company must have also achieved at least a rating of satisfactory record of meeting community credit needs under the Community Reinvestment Act during the depository institution's most recent examination.

A financial holding company ceasing to meet these standards is subject to a variety of restrictions, depending on the circumstances. If the Federal Reserve Board determines that any of the financial holding company's subsidiary depository institutions are either not well-capitalized or not well-managed, it must notify the financial holding company. Until compliance is restored, the Federal Reserve Board has broad discretion to impose appropriate limitations on the financial holding company's activities. If compliance is not restored within 180 days, the Federal Reserve Board may ultimately require the financial holding company to divest its depository institutions or in the

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alternative, to discontinue or divest any activities that are permitted only to non-financial holding company bank holding companies.

The potential restrictions are different if the lapse pertains to the Community Reinvestment Act requirement. In that case, until all the subsidiary institutions are restored to at least satisfactory Community Reinvestment Act rating status, the financial holding company may not engage, directly or through a subsidiary, in any of the additional activities permissible under the GLB Act or make additional acquisitions of companies engaged in the additional activities. However, completed acquisitions and additional activities and affiliations previously begun are left undisturbed, as the GLB Act does not require divestiture for this type of situation.

Financial holding companies may engage, directly or indirectly, in any activity that is determined to be (i) financial in nature, (ii) incidental to such financial activity, or (iii) complementary to a financial activity and does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally. The GLB Act specifically provides that the following activities have been determined to be financial in nature : (a) lending, trust and other banking activities; (b) insurance activities; (c) financial or economic advice or services; (d) pooled investments; (e) securities underwriting and dealing; (f) existing bank holding company domestic activities; (g) existing bank holding company foreign activities; and (h) merchant banking activities. The Corporation offers insurance agency services through its wholly-owned subsidiary, FirstBank Insurance Agency and through First Insurance Agency V. I., Inc., a subsidiary of FirstBank. In association with JP Morgan Chase, the Corporation, through FirstBank Puerto Rico Securities, Inc., a wholly owned subsidiary of FirstBank, also offers municipal bond underwriting services focused mainly on municipal and government bonds or obligations issued by the Puerto Rico government and its public corporations. Additionally, FirstBank Puerto Rico Securities, Inc. offers financial advisory services.

In addition, the GLB Act specifically gives the Federal Reserve Board the authority, by regulation or order, to expand the list of financial or incidental activities, but requires consultation with the Treasury, and gives the Federal Reserve Board authority to allow a financial holding company to engage in any activity that is complementary to a financial activity and does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally.

Under the GLB Act, if the Corporation fails to meet any of the requirements for being a financial holding company and is unable to resolve such deficiencies within certain prescribed periods of time, the Federal Reserve Board could require the Corporation to divest control of one or more of its depository institution subsidiaries or alternatively cease conducting financial activities that are not permissible for bank holding companies that are not financial holding companies.

Sarbanes-Oxley Act

The Sarbanes-Oxley Act of 2002 (SOA) implemented a range of corporate governance and accounting measures to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and to protect investors by improving the accuracy and reliability of disclosures under federal securities laws. In addition, SOA has established membership requirements and responsibilities for the audit committee, imposed restrictions on the relationship between the Corporation and external auditors, imposed additional responsibilities for the external financial statements on our chief executive officer and chief financial officer, expanded the disclosure requirements for corporate insiders, required management to evaluate its disclosure controls and procedures and its internal control over financial reporting, and required the auditors to issue a report on the internal control over financial reporting.

Since the 2004 Annual Report on Form 10-K, the Corporation has included in its annual report on Form 10-K its management assessment regarding the effectiveness of the Corporation s internal control over financial reporting. The internal control report includes a statement of management s responsibility for establishing and maintaining adequate internal control over financial reporting for the Corporation; management s assessment as to the effectiveness of the Corporation s internal control over financial reporting based on management s evaluation, as of year-end; and the framework used by management as criteria for evaluating the effectiveness of the Corporation s internal control over financial reporting. As of December 31, 2009, First BanCorp s management concluded that its

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internal control over financial reporting was effective. The Corporation's independent registered public accounting firm reached the same conclusion.

Emergency Economic Stabilization Act of 2008

On October 3, 2008, the Emergency Economic Stabilization Act of 2008 (the EESA) was signed into law. The EESA authorized the Treasury to access up to \$700 billion to protect the U.S. economy and restore confidence and stability to the financial markets. One such program under the Treasury Department's Troubled Asset Relief Program (TARP) was action by Treasury to make significant investments in U.S. financial institutions through the Capital Purchase Program (CPP). The Treasury's stated purpose in implementing the CPP was to improve the capitalization of healthy institutions, which would improve the flow of credit to businesses and consumers, and boost the confidence of depositors, investors, and counterparties alike. All federal banking and thrift regulatory agencies encouraged eligible institutions to participate in the CPP.

The Corporation applied for, and the Treasury approved, a capital purchase in the amount of \$400,000,000. The Corporation entered into a Letter Agreement with the Treasury, pursuant to which the Corporation issued and sold to the Treasury for an aggregate purchase price of \$400,000,000 in cash (i) 400,000 shares of the Series F Preferred Stock, and (2) the Warrant to purchase 5,842,259 shares of the Corporation's common stock at an exercise price of \$10.27 per share, subject to certain anti-dilution and other adjustments. The TARP transaction closed on January 16, 2009.

Under the terms of the Letter Agreement with the Treasury, (i) the Corporation amended its compensation, bonus, incentive and other benefit plans, arrangements and agreements (including severance and employment agreements) to the extent necessary to be in compliance with the executive compensation and corporate governance requirements of Section 111(b) of the Emergency Economic Stability Act of 2008 and applicable guidance or regulations issued by the Secretary of Treasury on or prior to January 16, 2009 and (ii) each Senior Executive Officer, as defined in the Purchase Agreement, executed a written waiver releasing Treasury and the Corporation from any claims that such officers may otherwise have as a result the Corporation's amendment of such arrangements and agreements to be in compliance with Section 111(b). Until such time as Treasury ceases to own any debt or equity securities of the Corporation acquired pursuant to the Purchase Agreement, the Corporation must maintain compliance with these requirements.

American Recovery and Reinvestment Act of 2009

On February 17, 2009, the Congress enacted the American Recovery and Reinvestment Act of 2009 (Stimulus Act). The Stimulus Act includes federal tax cuts, expansion of unemployment benefits and other social welfare provisions, and domestic spending in education, health care, and infrastructure, including energy sector. The Stimulus Act includes new provisions relating to compensation paid by institutions that receive government assistance under TARP, including institutions that have already received such assistance, effectively amending the existing compensation and corporate governance requirements of Section 111(b) of the EESA. The provisions include restrictions on the amounts and forms of compensation payable, provision for possible reimbursement of previously paid compensation and a requirement that compensation be submitted to non-binding say on pay shareholders votes.

On June 10, 2009, the Treasury issued regulations implementing the compensation requirements under ARRA, which amended the requirements of EESA. The regulations became applicable to existing and new TARP recipients upon publication in the Federal Register on June 15, 2009. The regulations make effective the compensation provisions of ARRA and include rules requiring: (i) review of prior compensation by a Special Master; (ii) restrictions on paying or accruing bonuses, retention awards or incentive compensation for certain employees; (iii) regular review of all employee compensation arrangements by the company's senior risk officer and compensation committee to ensure that the arrangements do not encourage unnecessary and excessive risk-taking or manipulation of reporting earnings; (iv) recoupment of bonus payments based on materially inaccurate information; (v) prohibition on severance or change in control payments for certain employees; (vi) adoption of policies and procedures to avoid excessive luxury expenses; and (vii) mandatory say on pay votes (which was effective beginning in February 2009). In addition, the regulations also introduce several additional requirements and restrictions, including: (i) Special Master review of ongoing compensation in certain situations; (ii) prohibition on

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tax gross-ups for certain employees; (iii) disclosure of perquisites; and (iv) disclosure regarding compensation consultants.

Homeowner Affordability and Stability Plan

On February 18, 2009, President Obama announced a comprehensive plan to help responsible homeowners avoid foreclosure by providing affordable and sustainable mortgage loans. The Homeowner Affordability and Stability Plan, a \$75 billion federal program, provides for a sweeping loan modification program targeted at borrowers who are at risk of foreclosure because their incomes are not sufficient to make their mortgage payments. It also includes refinancing opportunities for borrowers who are current on their mortgage payments but have been unable to refinance because their homes have decreased in value. Under the Homeowner Stability Initiative, Treasury will spend up to \$50 billion dollars to make mortgage payments affordable and sustainable for middle-income American families that are at risk of foreclosure. Borrowers who are delinquent on the mortgage for their primary residence and borrowers who, due to a loss of income or increase in expenses, are struggling to keep their payments current may be eligible for a loan modification. Under the Homeowner Affordability and Stability Plan, borrowers who are current on their mortgage but have been unable to refinance because their house has decreased in value may have the opportunity to refinance into a 30-year, fixed-rate loan. Through the program, Fannie Mae and Freddie Mac will allow the refinancing of mortgage loans that they hold in their portfolios or that they guarantee in their own mortgage-backed securities. Lenders were able to begin accepting refinancing applications on March 4, 2009. The Obama Administration announced on March 4, 2009 the new U.S. Department of the Treasury guidelines to enable servicers to begin modifications of eligible mortgages under the Homeowner Affordability and Stability Plan. The guidelines implement financial incentives for mortgage lenders to modify existing first mortgages and sets standard industry practice for modifications.

Temporary Liquidity Guarantee Program

The FDIC adopted the Temporary Liquidity Guarantee Program (TLGP) in October 2008 following a determination of systemic risk by the Secretary of the Treasury (after consultation with the President) that was supported by recommendations from the FDIC and the Board of Governors of the Federal Reserve System. The TLGP is part of a coordinated effort by the FDIC, the Treasury, and the Federal Reserve System to address unprecedented disruptions in the credit markets and the resultant difficulty of many financial institutions to obtain funds and to make loans to creditworthy borrowers. On October 23, 2008, the FDIC's Board of Directors (Board) authorized the publication in the Federal Register of an interim rule that outlined the structure of the TLGP. The interim rule was finalized and a final rule was published in the Federal Register on November 26, 2008. Designed to assist in the stabilization of the nation's financial system, the FDIC's TLGP is composed of two distinct components: the Debt Guarantee Program (DGP) and the Transaction Account Guarantee Program (TAG program). Under the DGP, the FDIC guarantees certain senior unsecured debt issued by participating entities. Under the TAG program, the FDIC guarantees all funds held in qualifying noninterest-bearing transaction accounts at participating insured depository institutions (IDIs). The DGP initially permitted participating entities to issue FDIC-guaranteed senior unsecured debt until June 30, 2009, with the FDIC's guarantee for such debt to expire on the earlier of the maturity of the debt (or the conversion date, for mandatory convertible debt) or June 30, 2012. To reduce the potential for market disruptions at the conclusion of the DGP and to begin the orderly phase-out of the program, on May 29, 2009 the Board issued a final rule that extended for four months the period during which certain participating entities could issue FDIC-guaranteed debt. All IDIs and those other participating entities that had issued FDIC-guaranteed debt on or before April 1, 2009 were permitted to participate in the extended DGP without application to the FDIC. Other participating entities that received approval from the FDIC also were permitted to participate in the extended DGP. The expiration of the guarantee period was also extended from June 30, 2012 to December 31, 2012. As a result, all such participating entities were permitted to issue FDIC-guaranteed debt through and including October 31, 2009, with the FDIC's guarantee expiring on the earliest of the debt's mandatory conversion date (for mandatory convertible debt), the stated maturity date, or December 31, 2012.

On October 20, 2009, the FDIC established a limited, six-month emergency guarantee facility upon expiration of the DGP. Under this emergency guarantee facility, certain participating entities can apply to the FDIC for permission to issue FDIC-guaranteed debt during the period starting October 31, 2009 through April 30, 2010. The fee for issuing

debt under the emergency facility will be at least 300 basis points, which the FDIC reserves the right to increase on a case-by-case basis, depending upon the risks presented by the issuing entity. The TAG Program has

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been extended until June 30, 2010. The cost of participating in the program increased after December 31, 2009. Separately, Congress extended the temporary increase in the standard coverage limit to \$250,000 until December 31, 2013. FirstBank currently participates in the TLGP solely through the TAG program.

USA Patriot Act

Under Title III of the USA Patriot Act, also known as the International Money Laundering Abatement and Anti-Terrorism Financing Act of 2001, all financial institutions are required to, among other things, identify their customers, adopt formal and comprehensive anti-money laundering programs, scrutinize or prohibit altogether certain transactions of special concern, and be prepared to respond to inquiries from U.S. law enforcement agencies concerning their customers and their transactions. Presently, only certain types of financial institutions (including banks, savings associations and money services businesses) are subject to final rules implementing the anti-money laundering program requirements of the USA Patriot Act.

Failure of a financial institution to comply with the USA Patriot Act's requirements could have serious legal and reputational consequences for the institutions. The Corporation has adopted appropriate policies, procedures and controls to address compliance with the USA Patriot Act and Treasury regulations.

Privacy Policies

Under Title V of the GLB Act, all financial institutions are required to adopt privacy policies, restrict the sharing of nonpublic customer data with parties at the customer's request and establish policies and procedures to protect customer data from unauthorized access. The Corporation and its subsidiaries have adopted policies and procedures in order to comply with the privacy provisions of the GLB Act and the Fair and Accurate Credit Transaction Act of 2003 and the regulations issued thereunder.

State Chartered Non-Member Bank and Banking Laws and Regulations in General

FirstBank is subject to regulation and examination by the OCIF and the FDIC, and is subject to certain requirements established by the Federal Reserve Board. The federal and state laws and regulations which are applicable to banks regulate, among other things, the scope of their businesses, their investments, their reserves against deposits, the timing and availability of deposited funds, and the nature and amount of collateral for certain loans. In addition to the impact of regulations, commercial banks are affected significantly by the actions of the Federal Reserve Board as it attempts to control the money supply and credit availability in order to influence the economy. Among the instruments used by the Federal Reserve Board to implement these objectives are open market operations in U.S. government securities, adjustments of the discount rate, and changes in reserve requirements against bank deposits. These instruments are used in varying combinations to influence overall economic growth and the distribution of credit, bank loans, investments and deposits. Their use also affects interest rates charged on loans or paid on deposits. The monetary policies and regulations of the Federal Reserve Board have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future. The effects of such policies upon our future business, earnings, and growth cannot be predicted.

References herein to applicable statutes or regulations are brief summaries of portions thereof which do not purport to be complete and which are qualified in their entirety by reference to those statutes and regulations. Any change in applicable laws or regulations may have a material adverse effect on the business of commercial banks, and bank holding companies, including FirstBank and the Corporation.

As a creditor and financial institution, FirstBank is subject to certain regulations promulgated by the Federal Reserve Board, including, without limitation, Regulation B (Equal Credit Opportunity Act), Regulation DD (Truth in Savings Act), Regulation E (Electronic Funds Transfer Act), Regulation F (Limits on Exposure to Other Banks), Regulation O (Loans to Executive Officers, Directors and Principal Shareholders), Regulation W (Transactions Between Member Banks and Their Affiliates), Regulation Z (Truth in Lending Act), Regulation CC (Expedited Funds Availability Act), Regulation X (Real Estate Settlement Procedures Act), Regulation BB (Community Reinvestment Act) and Regulation C (Home Mortgage Disclosure Act).

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During 2008, federal agencies adopted revisions to several rules and regulations that will impact lenders and secondary market activities. In 2008, the Federal Reserve Bank revised Regulation Z, adopted under the Truth in Lending Act (TILA) and the Home Ownership and Equity Protection Act (HOEPA), by adopting a final rule which prohibits unfair, abusive or deceptive home mortgage lending practices and restricts certain mortgage lending practices. The final rule also establishes advertisement standards and requires certain mortgage disclosures to be given to the consumers earlier in the transaction. The rule was effective in October 2009. The final rule regarding the TILA also includes amendments revising disclosures in connection with credit cards accounts and other revolving credit plans to ensure that information provided to customers is provided in a timely manner and in a form that is readily understandable.

There are periodic examinations by the OCIF and the FDIC of FirstBank to test the Bank's compliance with various statutory and regulatory requirements. This regulation and supervision establishes a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of the FDIC's insurance fund and depositors. The regulatory structure also gives the regulatory authorities discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. This enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease-and-desist or removal orders and to initiate injunctive actions against banking organizations and institution-affiliated parties. In general, these enforcement actions may be initiated for violations of laws and regulations and for engaging in unsafe or unsound practices. In addition, certain bank actions are required by statute and implementing regulations. Other actions or failure to act may provide the basis for enforcement action, including the filing of misleading or untimely reports with regulatory authorities.

Dividend Restrictions

The Corporation is subject to certain restrictions generally imposed on Puerto Rico corporations with respect to the declaration and payment of dividends (i.e., that dividends may be paid out only from the Corporation's net assets in excess of capital or, in the absence of such excess, from the Corporation's net earnings for such fiscal year and/or the preceding fiscal year). The Federal Reserve Board has also issued a policy statement that as a matter of prudent banking, a bank holding company should generally not maintain a given rate of cash dividends unless its net income available to common shareholders has been sufficient to fund fully the dividends and the prospective rate of earnings retention appears to be consistent with the organization's capital needs, asset quality, and overall financial condition. On February 24, 2009, the Federal Reserve published the *Applying Supervisory Guidance and Regulations on the Payment of Dividends, Stock Redemptions, and Stock Repurchases at Bank Holding Companies* (the *Supervisory Letter*) which discusses the ability of bank holding companies to declare dividends and to redeem or repurchase equity securities. The Supervisory Letter is generally consistent with prior Federal Reserve supervisory policies and guidance, although places greater emphasis on discussions with the regulators prior to dividend declarations and redemption or repurchase decisions even when not explicitly required by the regulations. The Federal Reserve provides that the principles discussed in the letter are applicable to all bank holding companies, but are especially relevant for bank holding companies that are either experiencing financial difficulties and/or receiving public funds under the Treasury's TARP Capital Purchase Program. To that end, the Supervisory Letter specifically addresses the Federal Reserve's supervisory considerations for TARP participants.

The Supervisory Letter provides that a board of directors should eliminate, defer, or severely limit dividends if: (i) the bank holding company's net income available to shareholders for the past four quarters, net of dividends paid during that period, is not sufficient to fully fund the dividends; (ii) the bank holding company's rate of earnings retention is inconsistent with capital needs and overall macroeconomic outlook; or (iii) the bank holding company will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios. The Supervisory Letter further suggests that bank holding companies should inform the Federal Reserve in advance of paying a dividend that: (i) exceeds the earnings for the quarter in which the dividend is being paid; or (ii) could result in a material adverse change to the organization's capital structure.

As of December 31, 2009, the principal source of funds for the Corporation's parent holding company is dividends declared and paid by its subsidiary, FirstBank. The ability of FirstBank to declare and pay dividends on its

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capital stock is regulated by the Puerto Rico Banking Law, the Federal Deposit Insurance Act (the FDIA), and FDIC regulations. In general terms, the Puerto Rico Banking Law provides that when the expenditures of a bank are greater than receipts, the excess of expenditures over receipts shall be charged against undistributed profits of the bank and the balance, if any, shall be charged against the required reserve fund of the bank. If the reserve fund is not sufficient to cover such balance in whole or in part, the outstanding amount must be charged against the bank's capital account. The Puerto Rico Banking Law provides that, until said capital has been restored to its original amount and the reserve fund to 20% of the original capital, the bank may not declare any dividends.

In general terms, the FDIA and the FDIC regulations restrict the payment of dividends when a bank is undercapitalized, when a bank has failed to pay insurance assessments, or when there are safety and soundness concerns regarding such bank.

In addition, the Purchase Agreement entered into with the Treasury contains limitations on 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), of common stock prior to October 14, 2008, which is \$0.07 per share. Also, upon issuance of the Series F Preferred Stock, the ability of the Corporation to purchase, redeem or otherwise acquire for consideration, any shares of its common stock, preferred stock or trust preferred securities is subject to restrictions, including limitations when the Corporation has not paid dividends. These restrictions will terminate on the earlier of (a) the third anniversary of the closing date of the issuance of the Series F Preferred Stock and (b) the date on which the Series F Preferred Stock has been redeemed in whole or Treasury has transferred all of the Series F Preferred Stock to third parties that are not affiliates of Treasury. The restrictions described in this paragraph are set forth in the Purchase Agreement.

On July 30, 2009, after reporting a net loss for the quarter ended June 30, 2009, the Corporation announced that the Board of Directors resolved to suspend the payment of the common and preferred dividends, including the TARP preferred dividends, effective with the preferred dividend payments for the month of August 2009.

Limitations on Transactions with Affiliates and Insiders

Certain transactions between financial institutions such as FirstBank and its affiliates are governed by Sections 23A and 23B of the Federal Reserve Act and by Regulation W. An affiliate of a financial institution is any corporation or entity, that controls, is controlled by, or is under common control with the financial institution. In a holding company context, the parent bank holding company and any companies which are controlled by such parent bank holding company are affiliates of the financial institution. Generally, Sections 23A and 23B of the Federal Reserve Act (i) limit the extent to which the financial institution or its subsidiaries may engage in covered transactions (defined below) with any one affiliate to an amount equal to 10% of such financial institution's capital stock and surplus, and contain an aggregate limit on all such transactions with all affiliates to an amount equal to 20% of such financial institution's capital stock and surplus and (ii) require that all covered transactions be on terms substantially the same, or at least as favorable to the financial institution or affiliate, as those provided to a non-affiliate. The term covered transaction includes the making of loans, purchase of assets, issuance of a guarantee and other similar transactions. In addition, loans or other extensions of credit by the financial institution to the affiliate are required to be collateralized in accordance with the requirements set forth in Section 23A of the Federal Reserve Act.

The GLB Act requires that financial subsidiaries of banks be treated as affiliates for purposes of Sections 23A and 23B of the Federal Reserve Act, but (i) the 10% capital limitation on transactions between the bank and such financial subsidiary as an affiliate is not applicable, and (ii) notwithstanding other provisions in Sections 23A and 23B, the investment by the bank in the financial subsidiary does not include retained earnings of the financial subsidiary. The GLB Act provides that: (1) any purchase of, or investment in, the securities of a financial subsidiary by any affiliate of the parent bank is considered a purchase or investment by the bank; and (2) if the Federal Reserve Board determines that such treatment is necessary, any loan made by an affiliate of the parent bank to the financial subsidiary is to be considered a loan made by the parent bank.

The Federal Reserve Board has adopted Regulation W which interprets the provisions of Sections 23A and 23B. The regulation unifies and updates staff interpretations issued over the years, incorporates several new interpretations and provisions (such as to clarify when transactions with an unrelated third party will be attributable

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to an affiliate), and addresses new issues arising as a result of the expanded scope of nonbanking activities engaged in by banks and bank holding companies in recent years and authorized for financial holding companies under the GLB Act.

In addition, Sections 22(h) and (g) of the Federal Reserve Act, implemented through Regulation O, place restrictions on loans to executive officers, directors, and principal stockholders. Under Section 22(h) of the Federal Reserve Act, loans to a director, an executive officer, a greater than 10% stockholder of a financial institution, and certain related interests of these, may not exceed, together with all other outstanding loans to such persons and affiliated interests, the financial institution's loans to one borrower limit, generally equal to 15% of the institution's unimpaired capital and surplus. Section 22(h) of the Federal Reserve Act also requires that loans to directors, executive officers, and principal stockholders be made on terms substantially the same as offered in comparable transactions to other persons and also requires prior board approval for certain loans. In addition, the aggregate amount of extensions of credit by a financial institution to insiders cannot exceed the institution's unimpaired capital and surplus. Furthermore, Section 22(g) of the Federal Reserve Act places additional restrictions on loans to executive officers.

Federal Reserve Board Capital Requirements

The Federal Reserve Board has adopted capital adequacy guidelines pursuant to which it assesses the adequacy of capital in examining and supervising a bank holding company and in analyzing applications to it under the Bank Holding Company Act. The Federal Reserve Board capital adequacy guidelines generally require bank holding companies to maintain total capital equal to 8% of total risk-adjusted assets, with at least one-half of that amount consisting of Tier I or core capital and up to one-half of that amount consisting of Tier II or supplementary capital. Tier I capital for bank holding companies generally consists of the sum of common stockholders' equity and perpetual preferred stock, subject in the case of the latter to limitations on the kind and amount of such perpetual preferred stock that may be included as Tier I capital, less goodwill and, with certain exceptions, other intangibles. Tier II capital generally consists of hybrid capital instruments, perpetual preferred stock that is not eligible to be included as Tier I capital, term subordinated debt and intermediate-term preferred stock and, subject to limitations, allowances for loan losses. Assets are adjusted under the risk-based guidelines to take into account different risk characteristics, with the categories ranging from 0% (requiring no additional capital) for assets such as cash to 100% for the bulk of assets, which are typically held by a bank holding company, including multi-family residential and commercial real estate loans, commercial business loans and commercial loans. Off-balance sheet items also are adjusted to take into account certain risk characteristics.

The federal bank regulatory agencies' risk-based capital guidelines for years have been based upon the 1988 capital accord (Basel I) of the Basel Committee, a committee of central bankers and bank supervisors from the major industrialized countries. This body develops broad policy guidelines for use by each country's supervisors in determining the supervisory policies they apply. In 2004, it proposed a new capital adequacy framework (Basel II) for large, internationally active banking organizations to replace Basel I. Basel II was designed to produce a more risk-sensitive result than its predecessor. However, certain portions of Basel II entail complexities and costs that were expected to preclude their practical application to the majority of U.S. banking organizations that lack the economies of scale needed to absorb the associated expenses.

Effective April 1, 2008, the U.S. federal bank regulatory agencies adopted Basel II for application to certain banking organizations in the United States. The new capital adequacy framework applies to organizations that: (i) have consolidated assets of at least \$250 billion; or (ii) have consolidated total on-balance sheet foreign exposures of at least \$10 billion; or (iii) are eligible to, and elect to, opt-in to the new framework even though not required to do so under clause (i) or (ii) above; or (iv) as a general matter, are subsidiaries of a bank or bank holding company that uses the new rule. During a two-year phase in period, organizations required or electing to apply Basel II will report their capital adequacy calculations separately under both Basel I and Basel II on a parallel run basis. Given the high thresholds noted above, FirstBank is not required to apply Basel II and does not expect to apply it in the foreseeable future.

On January 21, 2010, the federal banking agencies, including the Federal Reserve Board, issued a final risk-based regulatory capital rule related to the Financial Accounting Standards Board's adoption of amendments to the

accounting requirements relating to transfers of financial assets and variable interests in variable interest entities.

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These accounting standards make substantive changes to how banks account for securitized assets that are currently excluded from their balance sheets as of the beginning of the Corporation's 2010 fiscal year. The final regulatory capital rule seeks to better align regulatory capital requirements with actual risks. Under the final rule, banks affected by the new accounting requirements generally will be subject to higher minimum regulatory capital requirements.

The final rule permits banks to include without limit in tier 2 capital any increase in the allowance for lease and loan losses calculated as of the implementation date that is attributable to assets consolidated under the requirements of the variable interests accounting requirements. The rule provides an optional delay and phase-in for a maximum of one year for the effect on risk-based capital and the allowance for lease and loan losses related to the assets that must be consolidated as a result of the accounting change. The final rule also eliminates the risk-based capital exemption for asset-backed commercial paper assets. The transitional relief does not apply to the leverage ratio or to assets in conduits to which a bank provides implicit support. Banks will be required to rebuild capital and repair balance sheets to accommodate the new accounting standards by the middle of 2011.

Deposit Insurance

Under current FDIC regulations, each depository institution is assigned to a risk category based on capital and supervisory measures. In 2009, the FDIC revised the method for calculating the assessment rate for depository institutions by introducing several adjustments to an institution's initial base assessment rate. A depository institution is assessed premiums by the FDIC based on its risk category as adjusted and the amount of deposits held. Higher levels of banks failures over the past two years have dramatically increased resolution costs of the FDIC and depleted the deposit insurance fund. In addition, the amount of FDIC insurance coverage for insured deposits has been increased generally from \$100,000 per depositor to \$250,000 per depositor. In light of the increased stress on the deposit insurance fund caused by these developments, and in order to maintain a strong funding position and restore the reserve ratios of the deposit insurance fund, the FDIC: (i) imposed a special assessment in June, 2009, (ii) increased assessment rates of insured institutions generally, and (iii) required them to prepay on December 30, 2009 the premiums that are expected to become due over the next three years. FirstBank obtained a waiver from the FDIC to make such prepayment.

FDIC Capital Requirements

The FDIC has promulgated regulations and a statement of policy regarding the capital adequacy of state-chartered non-member banks like FirstBank. These requirements are substantially similar to those adopted by the Federal Reserve Board regarding bank holding companies, as described above.

The regulators require that banks meet a risk-based capital standard. The risk-based capital standard for banks requires the maintenance of total capital (which is defined as Tier I capital and supplementary (Tier 2) capital) to risk-weighted assets of 8%. In determining the amount of risk-weighted assets, weights used (ranging from 0% to 100%) are based on the risks inherent in the type of asset or item. The components of Tier I capital are equivalent to those discussed below under the 3.0% leverage capital standard. The components of supplementary capital include certain perpetual preferred stock, mandatorily convertible securities, subordinated debt and intermediate preferred stock and, generally, allowances for loan and lease losses. Allowance for loan and lease losses includable in supplementary capital is limited to a maximum of 1.25% of risk-weighted assets. Overall, the amount of capital counted toward supplementary capital cannot exceed 100% of core capital.

The capital regulations of the FDIC establish a minimum 3.0% Tier I capital to total assets requirement for the most highly-rated state-chartered, non-member banks, with an additional cushion of at least 100 to 200 basis points for all other state-chartered, non-member banks, which effectively will increase the minimum Tier I leverage ratio for such other banks from 4.0% to 5.0% or more. Under these regulations, the highest-rated banks are those that are not anticipating or experiencing significant growth and have well-diversified risk, including no undue interest rate risk exposure, excellent asset quality, high liquidity and good earnings and, in general, are considered a strong banking organization and are rated composite I under the Uniform Financial Institutions Rating System. Leverage or core capital is defined as the sum of common stockholders' equity including retained earnings, non-cumulative perpetual preferred stock and related surplus, and minority interests in consolidated subsidiaries, minus all intangible assets other than certain qualifying supervisory goodwill and certain purchased mortgage servicing rights.

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In August 1995, the FDIC published a final rule modifying its existing risk-based capital standards to provide for consideration of interest rate risk when assessing the capital adequacy of a bank. Under the final rule, the FDIC must explicitly include a bank's exposure to declines in the economic value of its capital due to changes in interest rates as a factor in evaluating a bank's capital adequacy. In June 1996, the FDIC adopted a joint policy statement on interest rate risk. Because market conditions, bank structure, and bank activities vary, the agency concluded that each bank needs to develop its own interest rate risk management program tailored to its needs and circumstances. The policy statement describes prudent principles and practices that are fundamental to sound interest rate risk management, including appropriate board and senior management oversight and a comprehensive risk management process that effectively identifies, measures, monitors and controls such interest rate risk.

Failure to meet capital guidelines could subject an insured bank to a variety of prompt corrective actions and enforcement remedies under the FDIA (as amended by Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), and the Riegle Community Development and Regulatory Improvement Act of 1994, including, with respect to an insured bank, the termination of deposit insurance by the FDIC, and certain restrictions on its business.

Under certain circumstances, a well-capitalized, adequately capitalized or undercapitalized institution may be treated as if the institution were in the next lower capital category. A depository institution is generally prohibited from making capital distributions (including paying dividends), or paying management fees to a holding company if the institution would thereafter be undercapitalized. Institutions that are adequately capitalized but not well-capitalized cannot accept, renew or roll over brokered deposits except with a waiver from the FDIC and are subject to restrictions on the interest rates that can be paid on such deposits. Undercapitalized institutions may not accept, renew or roll over brokered deposits.

The federal bank regulatory agencies are permitted or, in certain cases, required to take certain actions with respect to institutions falling within one of the three undercapitalized categories. Depending on the level of an institution's capital, the agency's corrective powers include, among other things:

- prohibiting the payment of principal and interest on subordinated debt;
- prohibiting the holding company from making distributions without prior regulatory approval;
- placing limits on asset growth and restrictions on activities;
- placing additional restrictions on transactions with affiliates;
- restricting the interest rate the institution may pay on deposits;
- prohibiting the institution from accepting deposits from correspondent banks; and

in the most severe cases, appointing a conservator or receiver for the institution.

A banking institution that is undercapitalized is required to submit a capital restoration plan, and such a plan will not be accepted unless, among other things, the banking institution's holding company guarantees the plan up to a certain specified amount. Any such guarantee from a depository institution's holding company is entitled to a priority of payment in bankruptcy.

As of December 31, 2009, FirstBank was well-capitalized. A bank's capital category, as determined by applying the prompt corrective action provisions of law, however, may not constitute an accurate representation of the overall financial condition or prospects of the Bank, and should be considered in conjunction with other available information regarding financial condition and results of operations.

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Set forth below are the Corporation's, FirstBank's capital ratios as of December 31, 2009, based on Federal Reserve and FDIC guidelines, respectively.

	First BanCorp	First Bank	Well-Capitalized Minimum
As of December 31, 2009			
Total capital (Total capital to risk-weighted assets)	13.44%	12.87%	10.00%
Tier 1 capital ratio (Tier 1 capital to risk-weighted assets)	12.16%	11.70%	6.00%
Leverage ratio(1)	8.91%	8.53%	5.00%

(1) Tier 1 capital to average assets.

Table of Contents***Activities and Investments***

The activities as principal and equity investments of FDIC-insured, state-chartered banks such as FirstBank are generally limited to those that are permissible for national banks. Under regulations dealing with equity investments, an insured state-chartered bank generally may not directly or indirectly acquire or retain any equity investments of a type, or in an amount, that is not permissible for a national bank.

Federal Home Loan Bank System

FirstBank is a member of the Federal Home Loan Bank (FHLB) system. The FHLB system consists of twelve regional Federal Home Loan Banks governed and regulated by the Federal Housing Finance Agency. The Federal Home Loan Banks serve as reserve or credit facilities for member institutions within their assigned regions. They are funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB system, and they make loans (advances) to members in accordance with policies and procedures established by the FHLB system and the board of directors of each regional FHLB.

FirstBank is a member of the FHLB of New York (FHLB-NY) and as such is required to acquire and hold shares of capital stock in that FHLB for a certain amount, which is calculated in accordance with the requirements set forth in applicable laws and regulations. FirstBank is in compliance with the stock ownership requirements of the FHLB-NY. All loans, advances and other extensions of credit made by the FHLB-NY to FirstBank are secured by a portion of FirstBank's mortgage loan portfolio, certain other investments and the capital stock of the FHLB-NY held by FirstBank.

Ownership and Control

Because of FirstBank's status as an FDIC-insured bank, as defined in the Bank Holding Company Act, First Bancorp, as the owner of FirstBank's common stock, is subject to certain restrictions and disclosure obligations under various federal laws, including the Bank Holding Company Act and the Change in Bank Control Act (the "CBCA"). Regulations pursuant to the Bank Holding Company Act generally require prior Federal Reserve Board approval for an acquisition of control of an insured institution (as defined in the Act) or holding company thereof by any person (or persons acting in concert). Control is deemed to exist if, among other things, a person (or persons acting in concert) acquires more than 25% of any class of voting stock of an insured institution or holding company thereof. Under the CBCA, control is presumed to exist subject to rebuttal if a person (or persons acting in concert) acquires more than 10% of any class of voting stock and either (i) the corporation has registered securities under Section 12 of the Securities Exchange Act of 1934, or (ii) no person will own, control or hold the power to vote a greater percentage of that class of voting securities immediately after the transaction. The concept of acting in concert is very broad and also is subject to certain rebuttable presumptions, including among others, that relatives, business partners, management officials, affiliates and others are presumed to be acting in concert with each other and their businesses. The regulations of the FDIC implementing the CBCA are generally similar to those described above.

The Puerto Rico Banking Law requires the approval of the OCIF for changes in control of a Puerto Rico bank. See Puerto Rico Banking Law.

Standards for Safety and Soundness

The FDIA, as amended by FDICIA and the Riegle Community Development and Regulatory Improvement Act of 1994, requires the FDIC and the other federal bank regulatory agencies to prescribe standards of safety and soundness, by regulations or guidelines, relating generally to operations and management, asset growth, asset quality, earnings, stock valuation, and compensation. The FDIC and the other federal bank regulatory agencies adopted, effective August 9, 1995, a set of guidelines prescribing safety and soundness standards pursuant to FDIA, as amended. The guidelines establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth and compensation, fees and benefits. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the

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amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director or principal shareholder.

Brokered Deposits

FDIC regulations adopted under the FDIA govern the receipt of brokered deposits by banks. Well-capitalized institutions are not subject to limitations on brokered deposits, while adequately-capitalized institutions are able to accept, renew or rollover brokered deposits only with a waiver from the FDIC and subject to certain restrictions on the interest paid on such deposits. Undercapitalized institutions are not permitted to accept brokered deposits. As of December 31, 2009, FirstBank was a well-capitalized institution and was therefore not subject to these limitations on brokered deposits. The FDIC and other bank regulators may also exercise regulatory discretion to enforce limits on the acceptance of brokered deposits if they have safety and soundness concerns as to an over reliance on such funding.

Puerto Rico Banking Law

As a commercial bank organized under the laws of the Commonwealth, FirstBank is subject to supervision, examination and regulation by the Commonwealth of Puerto Rico Commissioner of Financial Institutions (Commissioner) pursuant to the Puerto Rico Banking Law of 1933, as amended (the Banking Law). The Banking Law contains provisions governing the incorporation and organization, rights and responsibilities of directors, officers and stockholders as well as the corporate powers, lending limitations, capital requirements, investment requirements and other aspects of FirstBank and its affairs. In addition, the Commissioner is given extensive rule-making power and administrative discretion under the Banking Law.

The Banking Law authorizes Puerto Rico commercial banks to conduct certain financial and related activities directly or through subsidiaries, including the leasing of personal property and the operation of a small loan business.

The Banking Law requires every bank to maintain a legal reserve which shall not be less than twenty percent (20%) of its demand liabilities, except government deposits (federal, state and municipal) that are secured by actual collateral. The reserve is required to be composed of any of the following securities or combination thereof: (1) legal tender of the United States; (2) checks on banks or trust companies located in any part of Puerto Rico that are to be presented for collection during the day following the day on which they are received; (3) money deposited in other banks provided said deposits are authorized by the Commissioner, subject to immediate collection; (4) federal funds sold to any Federal Reserve Bank and securities purchased under agreements to resell executed by the bank with such funds that are subject to be repaid to the bank on or before the close of the next business day; and (5) any other asset that the Commissioner identifies from time to time.

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The Banking Law permits Puerto Rico commercial banks to make loans to any one person, firm, partnership or corporation, up to an aggregate amount of fifteen percent (15%) of the sum of: (i) the bank's paid-in capital; (ii) the bank's reserve fund; (iii) 50% of the bank's retained earnings; subject to certain limitations; and (iv) any other components that the Commissioner may determine from time to time. If such loans are secured by collateral worth at least twenty five percent (25%) more than the amount of the loan, the aggregate maximum amount may reach one third (33.33%) of the sum of the bank's paid-in capital, reserve fund, 50% of retained earnings and such other components that the Commissioner may determine from time to time. There are no restrictions under the Banking Law on the amount of loans that are wholly secured by bonds, securities and other evidence of indebtedness of the Government of the United States, or of the Commonwealth of Puerto Rico, or by bonds, not in default, of municipalities or instrumentalities of the Commonwealth of Puerto Rico. The revised classification of the mortgage-related transactions as secured commercial loans to local financial institutions described in the Corporation's restatement of previously issued financial statements (Form 10-K/A 2004) caused the mortgage-related transactions to be treated as two secured commercial loans in excess of the lending limitations imposed by the Banking Law. In this regard, FirstBank received a ruling from the Commissioner that results in FirstBank being considered in continued compliance with the lending limitations. The Puerto Rico Banking Law authorizes the Commissioner to determine other components which may be considered for purposes of establishing its lending limit, which components may lie outside the traditional elements mentioned in Section 17. After consideration of other components, the Commissioner authorized the Corporation to retain the secured loans to the two financial institutions as it believed that these loans were secured by sufficient collateral to diversify, disperse and significantly diffuse the risks connected to such loans thereby satisfying the safety and soundness considerations mandated by Section 28 of the Banking Law. In July 2009, FirstBank entered into a transaction with one of the institutions to purchase \$205 million in mortgage loans that served as collateral to the loan to this institution.

The Banking Law prohibits Puerto Rico commercial banks from making loans secured by their own stock, and from purchasing their own stock, unless such purchase is made pursuant to a stock repurchase program approved by the Commissioner or is necessary to prevent losses because of a debt previously contracted in good faith. The stock purchased by the Puerto Rico commercial bank must be sold by the bank in a public or private sale within one year from the date of purchase.

The Banking Law provides that no officers, directors, agents or employees of a Puerto Rico commercial bank may serve as an officer, director, agent or employee of another Puerto Rico commercial bank, financial corporation, savings and loan association, trust corporation, corporation engaged in granting mortgage loans or any other institution engaged in the money lending business in Puerto Rico. This prohibition is not applicable to the affiliates of a Puerto Rico commercial bank.

The Banking Law requires that Puerto Rico commercial banks prepare each year a balance summary of their operations, and submit such balance summary for approval at a regular meeting of stockholders, together with an explanatory report thereon. The Banking Law also requires that at least ten percent (10%) of the yearly net income of a Puerto Rico commercial bank be credited annually to a reserve fund. This credit is required to be done every year until such reserve fund shall be equal to the total paid-in-capital of the bank.

The Banking Law also provides that when the expenditures of a Puerto Rico commercial bank are greater than receipts, the excess of the expenditures over receipts shall be charged against the undistributed profits of the bank, and the balance, if any, shall be charged against the reserve fund, as a reduction thereof. If there is no reserve fund sufficient to cover such balance in whole or in part, the outstanding amount shall be charged against the capital account and no dividend shall be declared until said capital has been restored to its original amount and the reserve fund to twenty percent (20%) of the original capital.

The Banking Law requires the prior approval of the Commissioner with respect to a transfer of capital stock of a bank that results in a change of control of the bank. Under the Banking Law, a change of control is presumed to occur if a person or a group of persons acting in concert, directly or indirectly, acquire more than 5% of the outstanding voting capital stock of the bank. The Commissioner has interpreted the restrictions of the Banking Law as applying to acquisitions of voting securities of entities controlling a bank, such as a bank holding company. Under the Banking Law, the determination of the Commissioner whether to approve a change of control filing is final and

non-appealable.

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The Finance Board, which is composed of the Commissioner, the Secretary of the Treasury, the Secretary of Commerce, the Secretary of Consumer Affairs, the President of the Economic Development Bank, the President of the Government Development Bank, and the President of the Planning Board, has the authority to regulate the maximum interest rates and finance charges that may be charged on loans to individuals and unincorporated businesses in Puerto Rico. The current regulations of the Finance Board provide that the applicable interest rate on loans to individuals and unincorporated businesses, including real estate development loans but excluding certain other personal and commercial loans secured by mortgages on real estate properties, is to be determined by free competition. Accordingly, the regulations do not set a maximum rate for charges on retail installment sales contracts, small loans, and credit card purchases and set aside previous regulations which regulated these maximum finance charges. Furthermore, there is no maximum rate set for installment sales contracts involving motor vehicles, commercial, agricultural and industrial equipment, commercial electric appliances and insurance premiums.

International Banking Act of Puerto Rico (IBE Act)

The business and operations of First BanCorp Overseas (First BanCorp IBE , the IBE division of First BanCorp), FirstBank International Branch (FirstBank IBE , the IBE division of FirstBank) and FirstBank Overseas Corporation (the IBE subsidiary of FirstBank) are subject to supervision and regulation by the Commissioner. Under the IBE Act, certain sales, encumbrances, assignments, mergers, exchanges or transfers of shares, interests or participation(s) in the capital of an international banking entity (an IBE) may not be initiated without the prior approval of the Commissioner. The IBE Act and the regulations issued thereunder by the Commissioner (the IBE Regulations) limit the business activities that may be carried out by an IBE. Such activities are limited in part to persons and assets located outside of Puerto Rico.

Pursuant to the IBE Act and the IBE Regulations, each of First BanCorp IBE, FirstBank IBE and FirstBank Overseas Corporation must maintain books and records of all its transactions in the ordinary course of business. First BanCorp IBE, FirstBank IBE and FirstBank Overseas Corporation are also required thereunder to submit to the Commissioner quarterly and annual reports of their financial condition and results of operations, including annual audited financial statements.

The IBE Act empowers the Commissioner to revoke or suspend, after notice and hearing, a license issued thereunder if, among other things, the IBE fails to comply with the IBE Act, the IBE Regulations or the terms of its license, or if the Commissioner finds that the business or affairs of the IBE are conducted in a manner that is not consistent with the public interest.

Puerto Rico Income Taxes

Under the Puerto Rico Internal Revenue Code of 1994 (the Code), all companies are treated as separate taxable entities and are not entitled to file consolidated tax returns. The Corporation, and each of its subsidiaries are subject to a maximum statutory corporate income tax rate of 39% or an alternative minimum tax (AMT) on income earned from all sources, whichever is higher. The excess of AMT over regular income tax paid in any one year may be used to offset regular income tax in future years, subject to certain limitations. The Code provides for a dividend received deduction of 100% on dividends received from wholly owned subsidiaries subject to income taxation in Puerto Rico and 85% on dividends received from other taxable domestic corporations.

On March 9, 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%. This temporary measure is effective for tax years that commenced after December 31, 2008 and before January 1, 2012.

In computing the interest expense deduction, the Corporation's interest deduction will be reduced in the same proportion that the average exempt assets bear to the average total assets. Therefore, to the extent that the Corporation holds certain investments and loans that are exempt from Puerto Rico income taxation, part of its interest expense will be disallowed for tax purposes.

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The Corporation has maintained an effective tax rate lower than the maximum statutory tax rate of 40.95% during 2009 mainly by investing in government obligations and mortgage-backed securities exempt from U.S. and Puerto Rico income tax combined with income from the IBE units of the Corporation and the Bank and the Bank's subsidiary, FirstBank Overseas Corporation. The IBE, and FirstBank Overseas Corporation were created under the IBE Act, which provides for Puerto Rico tax exemption on net income derived by IBEs operating in Puerto Rico (except for year tax years commenced after December 31, 2008 and before January 1, 2012, in which all IBEs are subject to the special 5% tax on their net income not otherwise subject to tax pursuant to the PR Code, as provided by Act. No. 7). Pursuant to the provisions of Act No. 13 of January 8, 2004, the IBE Act was amended to impose income tax at regular rates on an IBE that operates as a unit of a bank, to the extent that the IBE net income exceeds 20% of the bank's total net taxable income (including net income generated by the IBE unit) for taxable years that commenced on July 1, 2005, and thereafter. These amendments apply only to IBEs that operate as units of a bank; they do not impose income tax on an IBE that operates as a subsidiary of a bank.

United States Income Taxes

The Corporation is also subject to federal income tax on its income from sources within the United States and on any item of income that is, or is considered to be, effectively connected with the active conduct of a trade or business within the United States. The U.S. Internal Revenue Code provides for tax exemption of portfolio interest received by a foreign corporation from sources within the United States; therefore, the Corporation is not subject to federal income tax on certain U.S. investments which qualify under the term "portfolio interest".

Insurance Operations Regulation

FirstBank Insurance Agency is registered as an insurance agency with the Insurance Commissioner of Puerto Rico and is subject to regulations issued by the Insurance Commissioner relating to, among other things, licensing of employees, sales, solicitation and advertising practices, and by the FED as to certain consumer protection provisions mandated by the GLB Act and its implementing regulations.

Community Reinvestment

Under the Community Reinvestment Act (CRA), federally insured banks have a continuing and affirmative obligation to meet the credit needs of their entire community, including low- and moderate-income residents, consistent with their safe and sound operation. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the type of products and services that it believes are best suited to its particular community, consistent with the CRA. The CRA requires the federal supervisory agencies, as part of the general examination of supervised banks, to assess the bank's record of meeting the credit needs of its community, assign a performance rating, and take such record and rating into account in their evaluation of certain applications by such bank. The CRA also requires all institutions to make public disclosure of their CRA ratings. FirstBank received a "satisfactory" CRA rating in their most recent examinations by the FDIC.

Mortgage Banking Operations

FirstBank is subject to the rules and regulations of the FHA, VA, FNMA, FHLMC, HUD and GNMA with respect to originating, processing, selling and servicing mortgage loans and the issuance and sale of mortgage-backed securities. Those rules and regulations, among other things, prohibit discrimination and establish underwriting guidelines that include provisions for inspections and appraisals, require credit reports on prospective borrowers and fix maximum loan amounts, and with respect to VA loans, fix maximum interest rates. Moreover, lenders such as FirstBank are required annually to submit to FHA, VA, FNMA, FHLMC, GNMA and HUD audited financial statements, and each regulatory entity has its own financial requirements. FirstBank's affairs are also subject to supervision and examination by FHA, VA, FNMA, FHLMC, GNMA and HUD at all times to assure compliance with the applicable regulations, policies and procedures. Mortgage origination activities are subject to, among others, the Equal Credit Opportunity Act, Federal Truth-in-Lending Act, and the Real Estate Settlement Procedures Act and the regulations promulgated thereunder which, among other things, prohibit discrimination and require the disclosure of certain basic information to mortgagors concerning credit terms and settlement costs. FirstBank is licensed by the Commissioner under the Puerto Rico Mortgage Banking Law, and as such is subject to

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regulation by the Commissioner, with respect to, among other things, licensing requirements and establishment of maximum origination fees on certain types of mortgage loan products.

Section 5 of the Puerto Rico Mortgage Banking Law requires the prior approval of the Commissioner for the acquisition of control of any mortgage banking institution licensed under such law. For purposes of the Puerto Rico Mortgage Banking Law, the term "control" means the power to direct or influence decisively, directly or indirectly, the management or policies of a mortgage banking institution. The Puerto Rico Mortgage Banking Law provides that a transaction that results in the holding of less than 10% of the outstanding voting securities of a mortgage banking institution shall not be considered a change in control.

Item 1A. Risk Factors

Certain risk factors that may affect the Corporation's future results of operations are discussed below.

RISK RELATING TO THE CORPORATION'S BUSINESS***Credit quality, which is continuing to deteriorate, may result in future additional losses.***

The quality of First BanCorp's credits has continued to be under pressure as a result of continued recessionary conditions in Puerto Rico and the state of Florida that have led to, among other things, higher unemployment levels, much lower absorption rates for new residential construction projects and further declines in property values. The Corporation's business depends on the creditworthiness of its customers and counterparties and the value of the assets securing its loans or underlying our investments. When the credit quality of the customer base materially decreases or the risk profile of a market, industry or group of customers changes materially, the Corporation's business, financial condition, allowance levels, asset impairments, liquidity, capital and results of operations are adversely affected.

While the Corporation has substantially increased our allowance for loan and lease losses in 2009, there is no certainty that it will be sufficient to cover future credit losses in the portfolio because of continued adverse changes in the economy, market conditions or events negatively affecting specific customers, industries or markets both in Puerto Rico and Florida. The Corporation periodically reviews the allowance for loan and lease losses for adequacy considering economic conditions and trends, collateral values and credit quality indicators, including charge-off experience and levels of past due loans and non-performing assets. First BanCorp's future results may be materially and adversely affected by worsening defaults and severity rates related to the underlying collateral.

The Corporation may have more credit risk and higher credit losses due to its construction loan portfolio.

The Corporation has a significant construction loan portfolio, in the amount of \$1.49 billion as of December 31, 2009, mostly secured by commercial and residential real estate properties. Due to their nature, these loans entail a higher credit risk than consumer and residential mortgage loans, since they are larger in size, concentrate more risk in a single borrower and are generally more sensitive to economic downturns. Rapidly changing collateral values, general economic conditions and numerous other factors continue to create volatility in the housing markets and have increased the possibility that additional losses may have to be recognized with respect to the Corporation's current nonperforming assets. Furthermore, given the current slowdown in the real estate market, the properties securing these loans may be difficult to dispose of if they are foreclosed.

The Corporation is subject to default risk on loans, which may adversely affect its results.

The Corporation is subject to the risk of loss from loan defaults and foreclosures with respect to the loans it originates. The Corporation establishes a provision for loan losses, which leads to reductions in its income from operations, in order to maintain its allowance for inherent loan losses at a level which its management deems to be appropriate based upon an assessment of the quality of the loan portfolio. Although the Corporation's management utilizes its best judgment in providing for loan losses, there can be no assurance that management has accurately estimated the level of inherent loan losses or that the Corporation will not have to increase its provision for loan losses in the future as a result of future increases in non-performing loans or for other reasons beyond its control.

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Any such increases in the Corporation's provision for loan losses or any loan losses in excess of its provision for loan losses would have an adverse effect on the Corporation's future financial condition and results of operations. Given the difficulties facing some of the Corporation's largest borrowers, the Corporation can give no assurance that these borrowers will continue to repay their loans on a timely basis or that the Corporation will continue to be able to accurately assess any risk of loss from the loans to these financial institutions.

Changes in collateral valuation for properties located in stagnant or distressed economies may require increased reserves.

Substantially all of the loan portfolio of the Corporation is located within the boundaries of the U.S. economy. Whether the collateral is located in Puerto Rico, the U.S. Virgin Islands, British Virgin Islands or the U.S. mainland, the performance of the Corporation's loan portfolio and the collateral value backing the transactions are dependent upon the performance of and conditions within each specific real estate market. Recent economic reports related to the real estate market in Puerto Rico indicate that certain pockets of the real estate market are subject to readjustments in value driven not by demand but more by the purchasing power of the consumers and general economic conditions. In South Florida, we have been seeing the negative impact associated with low absorption rates and property value adjustments due to overbuilding. A significant decline in collateral valuations for collateral dependent loans may require increases in the Corporation's specific provision for loan losses and an increase in the general valuation allowance. Any such increase would have an adverse effect on the Corporation's future financial condition and results of operations.

Worsening in the financial condition of critical counterparties may result in higher losses than expected.

The financial stability of several counterparties is critical for their continued financial performance on covenants that require the repurchase of loans, posting of collateral to reduce our credit exposure or replacement of delinquent loans. Many of these transactions expose the Corporation to credit risk in the event of a default by one of the Corporation's counterparties. Any such losses could adversely affect the Corporation's business, financial condition and results of operations.

Interest rate shifts may reduce net interest income.

Shifts in short-term interest rates may reduce net interest income, which is the principal component of the Corporation's earnings. Net interest income is the difference between the amount received by the Corporation on its interest-earning assets and the interest paid by the Corporation on its interest-bearing liabilities. When interest rates rise, the Corporation must pay more in interest on its liabilities while the interest earned on its assets does not rise as quickly. This may cause the Corporation's profits to decrease. This adverse impact on earnings is greater when the slope of the yield curve flattens, that is, when short-term interest rates increase more than long-term rates.

Increases in interest rates may reduce the value of holdings of securities.

Fixed-rate securities acquired by the Corporation are generally subject to decreases in market value when interest rates rise, which may require recognition of a loss (e.g., the identification of other-than-temporary impairment on its available for sale or held to maturity investments portfolio), thereby adversely affecting the results of operations. Market-related reductions in value also affect the capabilities of financing these securities.

Increases in interest rates may reduce demand for mortgage and other loans.

Higher interest rates increase the cost of mortgage and other loans to consumers and businesses and may reduce demand for such loans, which may negatively impact the Corporation's profits by reducing the amount of loan origination income.

Accelerated prepayments may adversely affect net interest income.

Net interest income of future periods may be affected by the acceleration in prepayments of mortgage-backed securities. Acceleration in the prepayments of mortgage-backed securities would lower yields on securities purchased at a premium, as the amortization of premiums paid upon acquisition of these securities would accelerate.

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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.

Also, net interest income in future periods might be affected by the Corporation's investment in callable securities. Approximately \$945 million of U.S. Agency debentures with an average yield of 5.82% were called during 2009. The Corporation re-invested the proceeds of the securities calls in callable Agency debentures of approximately 2.7 years average final maturity with a weighted average yield to maturity of 2.12%.

Decreases in interest rates may increase the probability embedded call options in investment securities are exercised. Future net interest income could be affected by the Corporation's holding of callable securities. The recent drop in long-term interest rates has the effect of increasing the probability of the exercise of embedded calls in U.S. Agency securities portfolio of approximately \$1.1 billion that if substituted with new lower-yield investments may negatively impact the Corporation's interest income.

Decreases in interest rates may reduce net interest income due to the current unprecedented re-pricing mismatch of assets and liabilities tied to short-term interest rates, which is referred to as basis risk.

Basis risk occurs when market rates for different financial instruments or the indices used to price assets and liabilities, change at different times or by different amounts. The liquidity crisis that erupted in late 2008, and that slowly began to subside during 2009 caused a wider than normal spread between brokered CD costs and LIBOR rates for similar terms. This in turn, has prevented the Corporation from capturing the full benefit of drops in interest rates as the Corporation's loan portfolio, funded by LIBOR-based brokered CDs, continue to maintain the same spread to short-term LIBOR rates, while the spread on brokered CD's widened. To the extent that such pressures fail to subside in the near future, the margin between the Corporation's LIBOR-based assets and LIBOR-based liabilities may compress and adversely affect net interest income.

If all or a significant portion of the unrealized losses in our investment securities portfolio on our consolidated balance sheet were determined to be other-than-temporarily impaired, we would recognize a material charge to our earnings and our capital ratios would be adversely affected.

As of December 31, 2009, the Corporation recognized \$1.7 million in other than temporary impairments. To the extent that any portion of the unrealized losses in its investment securities portfolio is determined to be other than temporary, and the loss is related to credit factors, the Corporation recognizes a charge to earnings in the quarter during which such determination is made and capital ratios could be adversely affected. If any such charge is significant, a rating agency might downgrade the Corporation's credit rating or put it on credit watch. Even if the Corporation does not determine that the unrealized losses associated with this portfolio requires an impairment charge, increases in these unrealized losses adversely affect the tangible common equity ratio, which may adversely affect credit rating agency and investor sentiment towards the Corporation. This negative perception also may adversely affect the Corporation's ability to access the capital markets or might increase the cost of capital.

As of December 31, 2009, the Corporation recognized other-than-temporary impairment on its private label MBS. Valuation and other-than-temporary impairment determinations will continue to be affected by external market factors including default rates, severity rates and macro-economic factors.

Downgrades in the Corporation's credit ratings could further increase the cost of borrowing funds.

Both, the Corporation and the Bank suffered credit rating downgrades in 2009. Fitch Ratings Ltd. (Fitch) currently rates the Corporation's long-term senior debt B-, six notches below investment grade. Standard and Poors rates the Corporation B, or five notches below investment grade. Moody's Investor Service (Moodys) rates FirstBank's long-term senior debt B1, and Standard & Poor's rates it B. The three rating agencies' outlooks on FirstBank and the Corporation's credit ratings are negative. The Corporation does not have any outstanding debt or derivative agreements that would be affected by a credit downgrade. The Corporation's liquidity is contingent upon its ability to obtain external sources of funding to finance its operations. Any future downgrades in credit ratings could put additional pressure on the Corporation's access to external funding and/or cause external funding to be more expensive, which could in turn adversely affect the results of operations. Changes in credit ratings may also

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affect the fair value of certain liabilities and unsecured derivatives, measured at fair value in the financial statements, for which the Corporation's own credit risk is an element considered in the fair value determination.

These debt and financial strength ratings are current opinions of the rating agencies. As such, they may be changed, suspended or withdrawn at any time by the rating agencies as a result of changes in, or unavailability of, information or based on other circumstances.

The Corporation's funding is significantly dependent on brokered deposits.

The Corporation's funding sources include core deposits, brokered deposits, borrowings from the Federal Home Loan Bank, borrowings from the Federal Reserve Bank and repurchase agreements with several counterparties.

A large portion of the Corporation's funding is retail brokered CDs issued by FirstBank. As of December 31, 2009, the Corporation had \$7.6 billion in brokered deposits outstanding, representing approximately 60% of our total deposits, and a reduction from \$8.4 billion at year end 2008. The Corporation issues brokered CDs to, among other things, pay operating expenses, maintain our lending activities, replace certain maturing liabilities, and to control interest rate risk.

FDIC regulations govern the issuance of brokered deposit instruments by banks. Well-capitalized institutions are not subject to limitations on brokered deposits, while adequately-capitalized institutions are able to accept, renew or rollover brokered deposits only with a waiver from the FDIC and subject to certain restrictions on the interest paid on such deposits. Undercapitalized institutions are not permitted to accept brokered deposits. As of December 31, 2009, the Corporation was a well-capitalized institution and was therefore not subject to these limitations on brokered deposits. If the Corporation became subject to such restrictions on its brokered deposits, the availability of such deposits would be limited and could, in turn, adversely affect the results of operations and the liquidity of the Corporation. The FDIC and other bank regulators may also exercise regulatory discretion to enforce limits on the acceptance of brokered deposits if they have safety and soundness concerns as to an over reliance on such funding.

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 enhances the Corporation's liquidity position, since the brokered CDs are insured by the FDIC up to regulatory limits and can be obtained faster compared to regular retail deposits. Demand for brokered CDs has recently increased as a result of the move by investors from riskier investments, such as equities, to federally guaranteed instruments such as brokered CDs and the recent increase in FDIC deposit insurance from \$100,000 to \$250,000. For the year ended December 31, 2009, the Corporation issued \$8.3 billion in brokered CDs (including rollover of short-term broker CDs and replacement of brokered CDs called) compared to \$9.8 billion for the 2008 year.

The average term to maturity of the retail brokered CDs outstanding as of December 31, 2009 was approximately 1.08 years. Approximately 1.55% of the principal value of these certificates is callable at the Corporation's option.

Another source of funding is Advances from the Discount Window of the Federal Reserve Bank of New York. Currently, the Corporation has \$800 million of borrowings outstanding with the Federal Reserve Bank. As part of the mechanisms to ease the liquidity crisis, during 2009 the Federal Reserve Bank encouraged banks to utilize the Discount Window as a source of funding. With the market conditions improving, the Federal Reserve announced in early 2010 its intention of withdrawing part of the economic stimulus measures, including replacing restrictions on the use of Discount Window borrowings, thereby returning to its function of lender of last resort.

The Corporation's funding sources may prove insufficient to replace deposits and support future growth.

The Corporation's banking subsidiary relies on customer deposits, brokered deposits and advances from the Federal Home Loan Bank (FHLB) to fund its operations. Although the Bank has historically been able to replace maturing deposits and advances if desired, no assurance can be given that it would be able to replace these funds in the future if the Corporation's financial condition or general market conditions were to change. The Corporation's

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financial flexibility will be severely constrained if the Bank is unable to maintain access to funding or if adequate financing is not available to accommodate future growth at acceptable interest rates. Finally, if the Corporation is required to rely more heavily on more expensive funding sources to support future growth, revenues may not increase proportionately to cover costs. In this case, profitability would be adversely affected. Although the Corporation considers such sources of funds adequate for its liquidity needs, the Corporation may seek additional debt financing in the future to achieve its long-term business objectives. There can be no assurance additional borrowings, if sought, would be available to the Corporation or, on what terms. If additional financing sources are unavailable or are not available on reasonable terms, growth and future prospects could be adversely affected.

Adverse credit market conditions may affect the Corporation's ability to meet liquidity needs.

The Corporation needs liquidity to, among other things, pay its operating expenses, interest on its debt and dividends on its capital stock, maintain its lending activities and replace certain maturing liabilities. Without sufficient liquidity, the Corporation may be forced to curtail its operations. The availability of additional financing will depend on a variety of factors such as market conditions, the general availability of credit and the Corporation's credit ratings and credit capacity. The Corporation's financial condition and cash flows could be materially affected by continued disruptions in financial markets.

Our controls and procedures may fail or be circumvented, our risk management policies and procedures may be inadequate, and operational risk could adversely affect our consolidated results of operations.

The Corporation may fail to identify and manage risks related to a variety of aspects of its business, including, but not limited to, operational risk, interest-rate risk, trading risk, fiduciary risk, legal and compliance risk, liquidity risk and credit risk. The Corporation has adopted various controls, procedures, policies and systems to monitor and manage risk. While the Corporation currently believes that its risk management process is effective, the Corporation cannot provide assurance that those controls, procedures, policies and systems will always be adequate to identify and manage the risks in the various businesses. In addition, the Corporation's businesses and the markets in which it operates are continuously evolving. The Corporation may fail to fully understand the implications of changes in its businesses or the financial markets and fail to adequately or timely enhance its risk framework to address those changes. If the Corporation's risk framework is ineffective, either because it fails to keep pace with changes in the financial markets or its businesses or for other reasons, the Corporation could incur losses, suffer reputational damage or find itself out of compliance with applicable regulatory mandates or expectations.

The Corporation may also be subject to disruptions from external events that are wholly or partially beyond its control, which could cause delays or disruptions to operational functions, including information processing and financial market settlement functions. In addition, our customers, vendors and counterparties could suffer from such events. Should these events affect us, or the customers, vendors or counterparties with which we conduct business, our consolidated results of operations could be negatively affected. When we record balance sheet reserves for probable loss contingencies related to operational losses, we may be unable to accurately estimate our potential exposure, and any reserves we establish to cover operational losses may not be sufficient to cover our actual financial exposure, which may have a material impact on our consolidated results of operations or financial condition for the periods in which we recognize the losses.

Competition for our employees is intense, and we may not be able to attract and retain the highly skilled people we need to support our business.

Our success depends, in large part, on our ability to attract and/or retain key people. Competition for the best people in most activities in which we engage can be intense, and we may not be able to hire people or retain them, particularly in light of uncertainty concerning evolving compensation restrictions applicable to banks but not applicable to other financial services firms. The unexpected loss of services of one or more of our key personnel could adversely affect our business because the loss of their skills, knowledge of our markets, and years of industry experience and, in some cases, because of the difficulty of promptly finding qualified replacement personnel. Similarly, the loss of key employees, either individually or as a group, can adversely affect our customers' perception of our ability to continue to manage certain types of investment management mandates.

Table of Contents***Banking regulators could take adverse action against the Corporation.***

The Corporation is subject to supervision and regulation by the FED. The Corporation is a bank holding company that qualifies as a financial holding corporation. As such, the Corporation is permitted to engage in a broader spectrum of activities than those permitted to bank holding companies that are not financial holding companies. To continue to qualify as a financial holding corporation, each of the Corporation's banking subsidiaries must continue to qualify as well-capitalized and well-managed. As of December 31, 2009, the Corporation and the Bank continue to satisfy all applicable capital guidelines. This, however, does not prevent banking regulators from taking adverse actions against the Corporation if they should conclude that such actions are warranted. If the Corporation were not to continue to qualify as a financial holding corporation, it might be required to discontinue certain activities and may be prohibited from engaging in new activities without prior regulatory approval. The Bank is subject to supervision and regulation by the FDIC, which conducts annual inspections, and, in Puerto Rico the OCIF. The primary regulators of the Corporation and the Bank have significant discretion and power to initiate enforcement actions for violations of laws and regulations and unsafe or unsound practices in the performance of their supervisory and enforcement duties and may do so even if the Corporation and the Bank continue to satisfy all capital requirements. Adverse action against the Corporation and/or the Bank by their primary regulators may affect their businesses.

Further increases in the FDIC deposit insurance premium may have a significant financial impact on the Corporation.

The FDIC insures deposits at FDIC insured financial institutions up to certain limits. The FDIC charges insured financial institutions premiums to maintain the Deposit Insurance Fund (the "DIF"). Current economic conditions have resulted in higher bank failures and expectations of future bank failures. In the event of a bank failure, the FDIC takes control of a failed bank and ensures payment of deposits up to insured limits (which have recently been increased) using the resources of the DIF. The FDIC is required by law to maintain adequate funding of the DIF, and the FDIC may increase premium assessments to maintain such funding.

On February 27, 2009, the FDIC determined that it would assess higher rates for institutions that relied significantly on secured liabilities or on brokered deposits but, for well-managed and well-capitalized banks, only when accompanied by rapid asset growth. On May 22, 2009, the FDIC adopted a final rule imposing a 5 basis-point special assessment on each insured depository institution's assets minus Tier 1 capital as of June 30, 2009. On November 12, 2009, the FDIC adopted a final rule imposing a 13-quarter prepayment of FDIC premiums due on December 30, 2009. Although FirstBank obtained a waiver from the FDIC to make such prepayment, the FDIC may further increase our premiums or impose additional assessments or prepayment requirements on the Corporation in the future.

The Corporation may not be able to recover all assets pledged to Lehman Brothers Special Financing, Inc.

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 constitutes 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 December 31, 2009 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 thereunder was required. The book value of pledged securities with Lehman as of December 31, 2009 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 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

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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 Barclay s Capital in New York. After Barclay s refusal to turn over the securities, the Corporation, during the month of December, 2009, filed a lawsuit against Barclay s Capital in federal court in New York demanding the return of the securities. While the Corporation believes it has valid reasons to support its claim for the return of the securities, there are no assurances that it will ultimately succeed in its litigation against Barclay s Capital to recover all or a substantial portion of the securities.

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. The Corporation can provide no assurances that it will be successful in recovering all or substantial portion of the securities through these proceedings.

Our businesses may be adversely affected by litigation.

From time to time, our customers, or the government on their behalf, may make claims and take legal action relating to our performance of fiduciary or contractual responsibilities. We may also face employment lawsuits or other legal claims. In any such claims or actions, demands for substantial monetary damages may be asserted against us resulting in financial liability or having an adverse effect on our reputation among investors or on customer demand for our products and services. We may be unable to accurately estimate our exposure to litigation risk when we record balance sheet reserves for probable loss contingencies. As a result, any reserves we establish to cover any settlements or judgments may not be sufficient to cover our actual financial exposure, which may have a material impact on our consolidated results of operations or financial condition.

In the ordinary course of our business, we are also subject to various regulatory, governmental and law enforcement inquiries, investigations and subpoenas. These may be directed generally to participants in the businesses in which we are involved or may be specifically directed at us. In regulatory enforcement matters, claims for disgorgement, the imposition of penalties and the imposition of other remedial sanctions are possible.

In view of the inherent difficulty of predicting the outcome of legal actions and regulatory matters, we cannot provide assurance as to the outcome of any pending matter or, if determined adversely against us, the costs associated with any such matter, particularly where the claimant seeks very large or indeterminate damages or where the matter presents novel legal theories, involves a large number of parties or is at a preliminary stage. The resolution of certain pending legal actions or regulatory matters, if unfavorable, could have a material adverse effect on our consolidated results of operations for the quarter in which such actions or matters are resolved or a reserve is established.

Further information with respect to the foregoing and our other ongoing litigation matters is provided in Legal Proceedings included under Item 3 herein.

Our businesses may be negatively affected by adverse publicity or other reputational harm.

Our relationships with many of our customers are predicated upon our reputation as a fiduciary and a service provider that adheres to the highest standards of ethics, service quality and regulatory compliance. Adverse publicity, regulatory actions, litigation, operational failures, the failure to meet customer expectations and other issues with respect to one or more of our businesses could materially and adversely affect our reputation, ability to attract and retain customers or sources of funding for the same or other businesses. Preserving and enhancing our reputation also depends on maintaining systems and procedures that address known risks and regulatory requirements, as well as our ability to identify and mitigate additional risks that arise due to changes in our businesses, the market places in which we operate, the regulatory environment and customer expectations. If any of these developments has a material adverse effect on our reputation, our business will suffer.

Table of Contents***Changes in accounting standards issued by the Financial Accounting Standards Board or other standard-setting bodies may adversely affect the Corporation's financial statements.***

The Corporation's financial statements are subject to the application of Generally Accepted Accounting Principles in the United States (GAAP), which is periodically revised and/or expanded. Accordingly, from time to time, the Corporation is required to adopt new or revised accounting standards issued by FASB. Market conditions have prompted accounting standard setters to promulgate new requirements that further interprets or seeks to revise accounting pronouncements related to financial instruments, structures or transactions as well as to issue new standards expanding disclosures. The impact of accounting pronouncements that have been issued but not yet implemented is disclosed in the Corporation's annual and quarterly reports on Form 10-K and Form 10-Q. An assessment of proposed standards is not provided as such proposals are subject to change through the exposure process and, therefore, the effects on the Corporation's financial statements cannot be meaningfully assessed. It is possible that future accounting standards that the Corporation is required to adopt could change the current accounting treatment that the Corporation applies to its consolidated financial statements and that such changes could have a material adverse effect on the Corporation's financial condition and results of operations.

The Corporation may need additional capital resources in the future and these capital resources may not be available when needed or at all.

Due to financial results during 2009 the Corporation may need to access the capital markets in order to raise additional capital in the future to absorb potential future credit losses due to the distressed economic environment, maintain adequate liquidity and capital resources or to finance future growth, investments or strategic acquisitions. The Corporation cannot provide assurances that such capital will be available on acceptable terms or at all. If the Corporation is unable to obtain additional capital, it may not be able to maintain adequate liquidity and capital resources or to finance future growth, make strategic acquisitions or investments.

Unexpected losses in future reporting periods may require the Corporation to adjust the valuation allowance against our deferred tax assets.

The Corporation evaluates the deferred tax assets for recoverability based on all available evidence. This process involves significant management judgment about assumptions that are subject to change from period to period based on changes in tax laws or variances between the future projected operating performance and the actual results. The Corporation is required to establish a valuation allowance for deferred tax assets if the Corporation determines, based on available evidence at the time the determination is made, that it is more likely than not that some portion or all of the deferred tax assets will not be realized. In determining the more-likely-than-not criterion, the Corporation evaluates all positive and negative evidence as of the end of each reporting period. Future adjustments, either increases or decreases, to the deferred tax asset valuation allowance will be determined based upon changes in the expected realization of the net deferred tax assets. The realization of the deferred tax assets ultimately depends on the existence of sufficient taxable income in either the carryback or carryforward periods under the tax law. Due to significant estimates utilized in establishing the valuation allowance and the potential for changes in facts and circumstances, it is reasonably possible that the Corporation will be required to record adjustments to the valuation allowance in future reporting periods. Such a charge could have a material adverse effect on our results of operations, financial condition and capital position.

If the Corporation's goodwill or amortizable intangible assets become impaired, it may adversely affect the operating results.

If the Corporation's goodwill or amortizable intangible assets become impaired the Corporation may be required to record a significant charge to earnings. Under generally accepted accounting principles, the Corporation reviews its amortizable intangible assets for impairment when events or changes in circumstances indicated the carrying value may not be recoverable. Goodwill is tested for impairment at least annually. Factors that may be considered a change in circumstances, indicating that the carrying value of the goodwill or amortizable intangible assets may not be recoverable, include reduced future cash flow estimates, and slower growth rates in the industry.

The goodwill impairment evaluation process requires the Corporation to make estimates and assumptions with regards to the fair value of the reporting units. Actual values may differ significantly from these estimates. Such differences could result in future impairment of goodwill that would, in turn, negatively impact the Corporation's

results of operations and the reporting unit where goodwill is recorded.

The Corporation conducted its annual evaluation of goodwill during the fourth quarter of 2009. This evaluation is a two-step process. The Step 1 evaluation of goodwill allocated to the Florida reporting unit, which is one level below the United States business segment, 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 December 31, 2009 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 of \$27 million, resulting in no goodwill impairment. If the Corporation is required to record a charge to earnings in the consolidated financial statements because an impairment of the goodwill or amortizable intangible assets is determined, the Corporation's results of operations could be adversely affected.

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RISK RELATED TO BUSINESS ENVIRONMENT AND OUR INDUSTRY

Difficult market conditions have affected the financial industry and may adversely affect the Corporation in the future.

Given that almost all of our business is in Puerto Rico and the United States and given the degree of interrelation between Puerto Rico's economy and that of the United States, the Corporation is particularly exposed to downturns in the U.S. economy. Dramatic declines in the U.S. housing market over the past few years, with falling home prices and increasing foreclosures, unemployment and under-employment, have negatively impacted the credit performance of mortgage loans and resulted in significant write-downs of asset values by financial institutions, including government-sponsored entities as well as major commercial banks and investment banks. These write-downs, initially of mortgage-backed securities but spreading to credit default swaps and other derivative and cash securities, in turn, have caused many financial institutions to seek additional capital from private and government entities, to merge with larger and stronger financial institutions and, in some cases, fail.

Reflecting concern about the stability of the financial markets in general and the strength of counterparties, many lenders and institutional investors have reduced or ceased providing funding to borrowers, including other financial institutions. This market turmoil and tightening of credit have led to an increased level of commercial and consumer delinquencies, erosion of consumer confidence, increased market volatility and widespread reduction of business activity in general. The resulting economic pressure on consumers and erosion of confidence in the financial markets has already adversely affected our industry and may adversely affect our business, financial condition and results of operations. The Corporation does not expect that the difficult conditions in the financial markets are likely to improve in the near future. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on the Corporation and other financial institutions. In particular, the Corporation may face the following risks in connection with these events:

The Corporation expects to face increased regulation of the financial industry resulting from the recent instability in capital markets, financial institutions and financial system in general. Compliance with such regulation may increase our costs and limit our ability to pursue business opportunities.

The Corporation's ability to assess the creditworthiness of our customers may be impaired if the models and approaches we use to select, manage, and underwrite the loans become less predictive of future behaviors.

The models used to estimate losses inherent in the credit exposure require difficult, subjective, and complex judgments, including forecasts of economic conditions and how these economic predictions might impair the ability of the borrowers to repay their loans, which may no longer be capable of accurate estimation and which may, in turn, impact the reliability of the models.

The Corporation's ability to borrow from other financial institutions or to engage in sales of mortgage loans to third parties (including mortgage loan securitization transactions with government-sponsored entities) on favorable terms, or at all could be adversely affected by further disruptions in the capital markets or other events, including deteriorating investor expectations.

Competitive dynamics in the industry could change as a result of consolidation of financial services companies in connection with current market conditions.

A prolonged economic slowdown or decline in the real estate market in the U.S. mainland could continue to harm the results of operations.

The residential mortgage loan origination business has historically been cyclical, enjoying periods of strong growth and profitability followed by periods of shrinking volumes and industry-wide losses. The market for residential mortgage loan originations is currently in decline and this trend could also reduce the level of mortgage

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loans the Corporation may produce in the future and adversely affect our business. During periods of rising interest rates, refinancing originations for many mortgage products tend to decrease as the economic incentives for borrowers to refinance their existing mortgage loans are reduced. In addition, the residential mortgage loan origination business is impacted by home values. Over the past eighteen months, residential real estate values in many areas of the U.S. mainland have decreased significantly, which has led to lower volumes and higher losses across the industry, adversely impacting our mortgage business.

The actual rates of delinquencies, foreclosures and losses on loans have been higher during the current economic slowdown. Rising unemployment, higher interest rates or declines in housing prices have had a greater negative effect on the ability of borrowers to repay their mortgage loans. Any sustained period of increased delinquencies, foreclosures or losses could continue to harm the Corporation's ability to sell loans, the prices the Corporation receives for loans, the values of mortgage loans held-for-sale or residual interests in securitizations, which could harm the Corporation's financial condition and results of operations. In addition, any material decline in real estate values would weaken the collateral loan-to-value ratios and increase the possibility of loss if a borrower defaults. In such event, the Corporation will be subject to the risk of loss on such real asset arising from borrower defaults to the extent not covered by third-party credit enhancement.

The Corporation's business concentration in Puerto Rico imposes risks.

The Corporation conducts its operations in a geographically concentrated area, as its main market is Puerto Rico. This imposes risks from lack of diversification in the geographical portfolio. The Corporation's financial condition and results of operations are highly dependent on the economic conditions of Puerto Rico, where adverse political or economic developments, natural disasters, and other events could affect among others, the volume of loan originations, increase the level of non-performing assets, increase the rate of foreclosure losses on loans, and reduce the value of the Corporation's loans and loan servicing portfolio.

The Corporation's credit quality may be adversely affected by Puerto Rico's current economic condition.

Beginning in March 2006 and continuing to today's date, a number of key economic indicators have showed that the economy of Puerto Rico has been in recession during that period of time.

Construction remained weak during 2009, as the Commonwealth's fiscal situation and decreasing public investment in construction projects affected the sector. During the period from January to December 2009, cement sales, an indicator of construction activity, declined by 29.6% as compared to 2008. As of October 2009, exports decreased by 6.8%, while imports decreased by 8.9%, a negative trade, which continues since the first negative trade balance of the last decade was registered in November 2006. Tourism activity also declined during 2009. Total hotel registrations for January to October 2009 declined 0.8% as compared to the same period for 2008. During January to September 2009 new vehicle sales decreased by 23.7%. In 2009, unemployment in Puerto Rico reached 15.0%, up 3.5 points compared with 2008.

On January 14, 2010 the Puerto Rico Planning Board announced the release of Puerto Rico's macroeconomic data for fiscal year 2009, ended June 30, 2009, as well as projected figures for fiscal year ending on June 30, 2010. The fiscal year 2009 showed a reduction of real GNP of -3.7%, while the projections for the fiscal year of 2010 point toward a positive growth of 0.7%. In general, the Puerto Rico economy continued its trend of decreasing growth, primarily due to weaker manufacturing, softer consumption and decreased government investment in construction.

The above economic concerns and uncertainty in the private and public sectors may also have an adverse effect on the credit quality of the Corporation's loan portfolios, as delinquency rates are expected to increase in the short-term, until the economy stabilizes. Also, a potential reduction in consumer spending may also impact growth in other interest and non-interest revenue sources of the Corporation.

Table of Contents***Rating downgrades on the Government of Puerto Rico's debt obligations may affect the Corporation's credit exposure.***

Even though Puerto Rico's economy is closely integrated to that of the U.S. mainland and its government and many of its instrumentalities are investment-grade rated borrowers in the U.S. capital markets, the current fiscal situation of the Government of Puerto Rico has led nationally recognized rating agencies to downgrade its debt obligations in the past.

Between May 2006 and mid-2009, the Government's bonds were downgraded as a result of factors such as the Government's inability to implement meaningful steps to curb operating expenditures, improve managerial and budgetary controls, high debt levels, chronic deficits, and the government's continued reliance on operating budget loans from the Government Development Bank for Puerto Rico.

In October and December 2009 both S&P and Moody's confirmed the Government's bond rating at BBB- and Baa3 with stable outlook, respectively. At present, both rating agencies maintain the stable outlooks for the general obligation bonds. In May 2009, S&P and Moody's upgraded the sales and use tax senior bonds from A+ to AA- and from A1 to Aa3, respectively due to a modification in its bond resolution.

It is uncertain how the financial markets may react to any potential future ratings downgrade in Puerto Rico's debt obligations. However, the fallout from the recent budgetary crisis and a possible ratings downgrade could adversely affect the value of Puerto Rico's Government obligations.

The failure of other financial institutions could adversely affect the Corporation.

The Corporation's ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial institutions are interrelated as a result of trading, clearing, counterparty and other relationships. The Corporation has exposure to different industries and counterparties, and routinely execute transactions with counterparties in the financial services industry, including brokers and dealers, commercial banks, investment banks, investment companies and other institutional clients. In certain of these transactions the Corporation is required to post collateral to secure the obligations to the counterparties. In the event of a bankruptcy or insolvency proceeding involving one of such counterparties, the Corporation may experience delays in recovering the assets posted as collateral or may incur a loss to the extent that the counterparty was holding collateral in excess of the obligation to such counterparty. There is no assurance that any such losses would not materially and adversely affect the Corporation's financial condition and results of operations.

In addition, many of these transactions expose the Corporation to credit risk in the event of a default by our counterparty or client. In addition, the credit risk may be exacerbated when the collateral held by the Corporation cannot be realized or is liquidated at prices not sufficient to recover the full amount of the loan or derivative exposure due to the Corporation. There is no assurance that any such losses would not materially and adversely affect the Corporation's financial condition and results of operations.

Legislative and regulatory actions taken now or in the future as a result of the current crisis in the financial industry may impact our business, governance structure, financial condition or results of operations.

Current economic conditions, particularly in the financial markets, have resulted in government regulatory agencies and political bodies placing increased focus and scrutiny on the financial services industry. The U.S. government has intervened on an unprecedented scale, responding to what has been commonly referred to as the financial crisis, by temporarily enhancing the liquidity support available to financial institutions, establishing a commercial paper funding facility, temporarily guaranteeing money market funds and certain types of debt issuances and increasing insurance on bank deposits.

These programs have subjected financial institutions, particularly those participating in the U.S. Treasury's Troubled Asset Relief Program (the TARP), to additional restrictions, oversight and costs. In addition, new proposals for legislation continue to be introduced in the U.S. Congress that could further substantially increase regulation of the financial services industry, impose restrictions on the operations and general ability of firms within

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the industry to conduct business consistent with historical practices, including in the areas of compensation, interest rates, financial product offerings and disclosures, and have an effect on bankruptcy proceedings with respect to consumer residential real estate mortgages, among other things. Federal and state regulatory agencies also frequently adopt changes to their regulations or change the manner in which existing regulations are applied.

The Corporation also faces increased regulation and regulatory scrutiny as a result of our participation in the TARP. In January 2009, the Corporation issued Series F Preferred Stock and warrants to purchase the Corporation's Common Stock to the U.S. Treasury under the TARP. Pursuant to the terms of this issuance, the Corporation is prohibited from increasing the dividend rate on our Common Stock in an amount exceeding the last quarterly cash dividend paid per share, or the amount publicly announced (if lower), of Common Stock prior to October 14, 2008, which was \$0.07 per share, without approval. Furthermore, as long as Series F Preferred Stock issued to the U.S. Treasury is outstanding, dividend payments and repurchases or redemptions relating to certain equity securities, including the Corporation's Common Stock, are prohibited unless all accrued and unpaid dividends are paid on Series F Preferred Stock, subject to certain limited exceptions.

On January 21, 2009, the U.S. House of Representatives approved legislation amending the TARP provisions of Emergency Economic Stabilization Act (EESA) to include quarterly reporting requirements with respect to lending activities, examinations by an institution's primary federal regulator of the use of funds and compliance with program requirements, restrictions on acquisitions by depository institutions receiving TARP funds and authorization for the U.S. Treasury to have an observer at board meetings of recipient institutions, among other things. On February 17, 2009, President Obama signed into law the American Reinvestment and Recovery Act of 2009 (the ARRA). The ARRA contains expansive new restrictions on executive compensation for financial institutions and other companies participating in the TARP. The ARRA amends the executive compensation and corporate governance provisions of EESA. In doing so, it continues all the same compensation and governance restrictions and adds substantially to restrictions in several areas. In addition, on June 10, 2009, the U.S. Treasury issued regulations implementing the compensation requirements under the ARRA. The regulations became applicable to existing TARP recipients upon publication in the Federal Register on June 15, 2009. The aforementioned compensation requirements and restrictions may adversely affect our ability to retain or hire senior bank officers.

The U.S. House of Representatives approved a regulatory reform package on December 11, 2009 (H.R. 4173). The U.S. Senate is also expected to consider financial reform legislation during 2010. H.R. 4173 and a Discussion Draft of legislation that may be introduced in the U.S. Senate contain provisions, which would, among other things, establish a Consumer Financial Protection Agency, establish a systemic risk regulator, consolidate federal bank regulators and give shareholders an advisory vote on executive compensation. Separate legislative proposals call for partial repeal of the Gramm-Leach-Bliley Act of 1999 (the GLB Act), which is discussed below.

The Obama administration is also requesting Congressional action to limit the growth of the largest U.S. financial firms and to bar banks and bank-related companies from engaging in proprietary trading and from owning, investing in or sponsoring hedge funds or private equity funds. A separate legislative proposal would impose a new fee or tax on U.S. financial institutions as part of the 2010 budget plans in an effort to reduce the anticipated budget deficit and to recoup losses anticipated from the TARP. Such an assessment is estimated to be 15-basis points, levied against bank assets minus Tier 1 capital and domestic deposits. It appears that this fee or tax would be assessed only against the 50 or so largest financial institutions in the U.S., which are those with more than \$50 billion in assets, and therefore would not directly affect First BanCorp. However, the large banks that are affected by the tax may choose to seek additional deposit funding in the marketplace, driving up the cost of deposits for all banks. The administration has also considered a transaction tax on trades of stock in financial institutions and a tax on executive bonuses.

The U.S. Congress has also recently adopted additional consumer protection laws such as the Credit Card Accountability Responsibility and Disclosure Act of 2009, and the Federal Reserve has adopted numerous new regulations addressing banks' credit card, overdraft and mortgage lending practices. Additional consumer protection legislation and regulatory activity is anticipated in the near future.

Internationally, both the Basel Committee on Banking Supervision (the Basel Committee) and the Financial Stability Board (established in April 2009 by the Group of Twenty Finance Ministers and Central Bank Governors to take action to strengthen regulation and supervision of the financial system with greater international consistency,

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cooperation and transparency) have committed to raise capital standards and liquidity buffers within the banking system.

Such proposals and legislation, if finally adopted, would change banking laws and our operating environment and that of our subsidiaries in substantial and unpredictable ways. The Corporation cannot determine whether such proposals and legislation will be adopted, or the ultimate effect that such proposals and legislation, if enacted, or regulations issued to implement the same, would have upon its financial condition or results of operations.

Monetary policies and regulations of the Federal Reserve could adversely affect our business, financial condition and results of operations.

In addition to being affected by general economic conditions, the earnings and growth of First BanCorp are affected by the policies of the Federal Reserve. An important function of the Federal Reserve is to regulate the money supply and credit conditions. Among the instruments used by the Federal Reserve to implement these objectives are open market operations in U.S. Government securities, adjustments of the discount rate and changes in reserve requirements against bank deposits. These instruments are used in varying combinations to influence overall economic growth and the distribution of credit, bank loans, investments and deposits. Their use also affects interest rates charged on loans or paid on deposits.

On January 6, 2010, the member agencies of the Federal Financial Institutions Examination Council (the FFIEC), which includes the Federal Reserve, issued an interest rate risk advisory reminding banks to maintain sound practices for managing interest rate risk, particularly in the current environment of historically low short-term interest rates.

The monetary policies and regulations of the Federal Reserve have had a significant effect on the operating results of commercial banks in the past and are expected to continue to do so in the future. The effects of such policies upon our business, financial condition and results of operations cannot be predicted.

The Corporation faces extensive and changing government regulation, which may increase our costs of and expose us to risks related to compliance.

Most of our businesses are subject to extensive regulation by multiple regulatory bodies. These regulations may affect the manner and terms of delivery of our services. If we do not comply with governmental regulations, we may be subject to fines, penalties, lawsuits or material restrictions on our businesses in the jurisdiction where the violation occurred, which may adversely affect our business operations. Changes in these regulations can significantly affect the services that we are asked to provide as well as our costs of compliance with such regulations. In addition, adverse publicity and damage to our reputation arising from the failure or perceived failure to comply with legal, regulatory or contractual requirements could affect our ability to attract and retain customers. In recent years, regulatory oversight and enforcement have increased substantially, imposing additional costs and increasing the potential risks associated with our operations. If this regulatory trend continues, it could adversely affect our operations and, in turn, our consolidated results of operations.

We are subject to regulatory capital adequacy guidelines, and if we fail to meet these guidelines our business and financial condition may be adversely affected.

Under regulatory capital adequacy guidelines, and other regulatory requirements, the Corporation and the Bank must meet guidelines that include quantitative measures of assets, liabilities and certain off-balance sheet items, subject to qualitative judgments by regulators regarding components, risk weightings and other factors. If we fail to meet these minimum capital guidelines and other regulatory requirements, our business and financial condition will be materially and adversely affected. If we fail to maintain well-capitalized status under the regulatory framework, or are deemed to be not well-managed under regulatory exam procedures, or if we experience certain regulatory violations, our status as a financial holding company and our related eligibility for a streamlined review process for acquisition proposals, and our ability to offer certain financial products will be compromised.

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The imposition of additional property tax payments in Puerto Rico may further deteriorate our commercial, consumer and mortgage loan portfolios.

On March 9, 2009, the Governor of Puerto Rico signed into law the Special Act Declaring a State of Fiscal Emergency and Establishing an Integral Plan of Fiscal Stabilization to Save Puerto Rico's Credit, Act No. 7 (the Act). The Act imposes a series of temporary and permanent measures, including the imposition of a 0.591% special tax applicable to properties used for residential (excluding those exempt as detailed in the Act) and commercial purposes, and payable to the Puerto Rico Treasury Department. This temporary measure will be effective for tax years that commenced after June 30, 2009 and before July 1, 2012. The imposition of this special property tax could adversely affect the disposable income of borrowers from the commercial, consumer and mortgage loan portfolios and may cause an increase in our delinquency and foreclosure rates.

RISKS RELATING TO AN INVESTMENT IN THE CORPORATION'S SECURITIES

The market price of the Corporation's common stock may be subject to significant fluctuations and volatility.

The stock markets have recently experienced high levels of volatility. These market fluctuations have adversely affected, and may continue to adversely affect, the trading price of the Corporation's common stock. In addition, the market price of the Corporation's common stock has been subject to significant fluctuations and volatility because of factors specifically related to its businesses and may continue to fluctuate or further decline. Factors that could cause fluctuations, volatility or further decline in the market price of the Corporation's common stock, many of which could be beyond its control, include the following:

- changes or perceived changes in the condition, operations, results or prospects of the Corporation's businesses and market assessments of these changes or perceived changes;

- announcements of strategic developments, acquisitions and other material events by the Corporation or its competitors;

- changes in governmental regulations or proposals, or new governmental regulations or proposals, affecting the Corporation, including those relating to the recent financial crisis and global economic downturn and those that may be specifically directed to the Corporation;

- the continued decline, failure to stabilize or lack of improvement in general market and economic conditions in the Corporation's principal markets;

- the departure of key personnel;

- changes in the credit, mortgage and real estate markets;

- operating results that vary from the expectations of management, securities analysts and investors; and

- operating and stock price performance of companies that investors deem comparable to the Corporation.

Our suspension of dividends could adversely affect our stock price and result in the expansion of our board of directors.

In March of 2009, the Board of Governors of the Federal Reserve System issued a supervisory guidance letter intended to provide direction to bank holding companies (BHCs) on the declaration and payment of dividends, capital redemptions and capital repurchases by BHCs in the context of their capital planning process. The letter reiterates the long-standing Federal Reserve supervisory policies and guidance to the effect that BHCs should only pay dividends from current earnings. More specifically, the letter heightens expectations that BHCs will inform and consult with the Federal Reserve supervisory staff on the declaration and payment of dividends that exceed earnings for the period for which a dividend is being paid. In consideration of the financial results reported for the second quarter ended June 30, 2009, the Corporation decided, as a matter of prudent fiscal management and following the Federal Reserve guidance, to suspend payment of common stock dividends and dividends on all series of preferred stock. The Corporation

cannot anticipate if and when the payment of dividends might be reinstated.

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This suspension could adversely affect the Corporation's stock price. Further, in general, if dividends on our preferred stock are not paid for six quarterly dividend periods or more, the authorized number of directors of the board will be increased by two and the preferred stockholders will have the right to elect two additional members of the Corporation's board of directors until all accrued and unpaid dividends for all past dividend periods have been declared and paid in full.

Dividends on the Corporation's common stock have been suspended and a holder may not receive funds in connection with its investment in our common stock without selling its shares of common stock.

Holders of common stock are only entitled to receive such dividends as the Corporation's board of directors may declare out of funds legally available for such payments. The Corporation announced the suspension of dividend payments on its common stock. In general, so long as any shares of preferred stock remain outstanding and until the Corporation satisfies various Federal regulatory considerations, the Corporation cannot declare, set apart or pay any dividends on shares of the Corporation's common stock unless all accrued and unpaid dividends on its preferred stock for the twelve monthly dividend periods ending on the immediately preceding dividend payment date have been paid or are paid contemporaneously and the full monthly dividend on its preferred stock for the then current month has been or is contemporaneously declared and paid or declared and set apart for payment. Furthermore, prior to January 16, 2012, unless the Corporation has redeemed all of the shares of Series F Preferred Stock (or any successor security) or the U.S. Treasury has transferred all of Series F Preferred Stock (or any successor security) to third parties, the consent of the U.S. Treasury will be required for the Corporation to, among other things, increase the dividend rate per share of Common Stock above \$0.07 per share or to repurchase or redeem equity securities, including the Corporation's common stock, subject to certain limited exceptions. This could adversely affect the market price of the Corporation's common stock. Also, the Corporation is a bank holding company and its ability to declare and pay dividends is dependent on certain Federal regulatory considerations, including the guidelines of the Federal Reserve regarding capital adequacy and dividends. Moreover, the Federal Reserve and the FDIC have issued policy statements stating that bank holding companies and insured banks should generally pay dividends only out of current operating earnings. In the current financial and economic environment, the Federal Reserve has indicated that bank holding companies should carefully review their dividend policy and has discouraged dividend pay-out ratios that are at the 100% or higher level unless both asset quality and capital are very strong.

In addition, the terms of the Corporation's outstanding junior subordinated debt securities held by trusts that issue trust preferred securities prohibit the Corporation from declaring or paying any dividends or distributions on its capital stock, including its common stock and preferred stock, or purchasing, acquiring, or making a liquidation payment on such stock, if the Corporation has given notice of its election to defer interest payments but the related deferral period has not yet commenced or a deferral period is continuing.

Offerings of debt, which would be senior to the common stock upon liquidation and/or to preferred equity securities, which may be senior to the common stock for purposes of dividend distributions or upon liquidation, may adversely affect the market price of the common stock.

The Corporation may attempt to increase its capital resources or, if its or the capital ratios of FirstBank fall below the required minimums, the Corporation or FirstBank could be forced to raise additional capital by making additional offerings of debt or preferred equity securities, including medium-term notes, trust preferred securities, senior or subordinated notes and preferred stock. Upon liquidation, holders of debt securities and shares of preferred stock and lenders with respect to other borrowings will receive distributions of the Corporation's available assets prior to the holders of the common stock. Additional equity offerings may dilute the holdings of existing stockholders or reduce the market price of the common stock, or both.

The Corporation's board of directors is authorized to issue one or more classes or series of preferred stock from time to time without any action on the part of the stockholders. The Corporation's board of directors also has the power, without stockholder approval, to set the terms of any such classes or series of preferred stock that may be issued, including voting rights, dividend rights and preferences over the common stock with respect to dividends or upon the Corporation's dissolution, winding up and liquidation and other terms. If the Corporation issues preferred shares in the future that have a preference over the common stock with respect to the payment of dividends or upon liquidation, or if the Corporation issues preferred shares with voting rights that dilute the voting power of the

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common stock, the rights of holders of the common stock or the market price of the common stock could be adversely affected.

There may be future dilution of the Corporation's common stock.

In January 2009, in connection with the U.S. Treasury's TARP Capital Purchase Program, established as part of the Emergency Economic Stabilization Act of 2008, the Corporation issued to the U.S. Treasury 400,000 shares of its Fixed Rate Cumulative Perpetual Preferred Stock, Series F, \$1,000 liquidation preference value per share. In connection with this investment, the Corporation also issued to the U.S. Treasury a warrant to purchase 5,842,259 shares of the Corporation's common stock (the Warrant) at an exercise price of \$10.27 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. In addition, in connection with its sale of 9,250,450 shares of common stock to the Bank of Nova Scotia (BNS), the Corporation agreed to give BNS an anti-dilution right and a right of first refusal when the Corporation sells shares of common stock to third parties. The possible future issuance of equity securities through the exercise of the Warrant or to BNS as a result of its rights 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 6% of the Corporation's outstanding shares of common stock as of December 31, 2009 and BNS owns 10% of the Corporation's shares of common stock);

- 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.

Also, recent increases in the allowance for loan and lease losses resulted in a reduction in the amount of the Corporation's tangible common equity. Given the focus on tangible common equity by regulatory authorities and rating agencies, the Corporation may be required to raise additional capital through the issuance of additional common stock in future periods to increase that tangible common equity. However, no assurance can be given that the Corporation will be able to raise additional capital. An increase in the Corporation's capital through an issuance of common stock could have a dilutive effect on the existing holders of our Common Stock and may adversely affect its market price.

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Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

As of December 31, 2009, First BanCorp owned the following three main offices located in Puerto Rico:

Main offices:

- Headquarters Located at First Federal Building, 1519 Ponce de León Avenue, Santurce, Puerto Rico, a 16 story office building. Approximately 60% of the building, an underground three level parking lot and an adjacent parking lot are owned by the Corporation.
- EDP & Operations Center A five-story structure located at 1506 Ponce de León Avenue, Santurce, Puerto Rico. These facilities are fully occupied by the Corporation.
- Consumer Lending Center A three-story building with a three-level parking lot located at 876 Muñoz Rivera Avenue, Hato Rey, Puerto Rico. These facilities are fully occupied by the Corporation.
- In addition, during 2006, First BanCorp purchased a building located on 1130 Muñoz Rivera Avenue, Hato Rey, Puerto Rico. These facilities are being renovated and expanded to accommodate branch operations, data processing, administrative and certain headquarter offices. FirstBank expects to commence occupancy in summer 2010.

The Corporation owned 24 branch and office premises and auto lots and leased 117 branch premises, loan and office centers and other facilities. In certain situations, financial services such as mortgage, insurance businesses and commercial banking services are located in the same building. All of these premises are located in Puerto Rico, Florida and in the U.S. and British Virgin Islands. Management believes that the Corporation's properties are well maintained and are suitable for the Corporation's business as presently conducted.

Item 3. Legal Proceedings

The Corporation and its subsidiaries are defendants in various lawsuits arising in the ordinary course of business. In the opinion of the Corporation's management the pending and threatened legal proceedings of which management is aware will not have a material adverse effect on the financial condition or results of operations of the Corporation.

Item 4. Reserved

Table of Contents**PART II****Item 5. Market for Registrant's Common Equity and Related Stockholder Matters and Issuer Purchases of Equity Securities****Information about Market and Holders**

The Corporation's common stock is traded on the New York Stock Exchange (NYSE) under the symbol FBP. On December 31, 2009, there were 540 holders of record of the Corporation's common stock.

The following table sets forth, for the calendar quarters indicated, the high and low closing sales prices and the cash dividends declared on the Corporation's common stock during such periods.

Quarter Ended	High	Low	Last	Dividends per Share
2009:				
December	\$ 2.88	\$ 1.51	\$ 2.30	\$
September	4.20	3.01	3.05	
June	7.55	3.95	3.95	0.07
March	11.05	3.63	4.26	0.07
2008:				
December	\$12.17	\$ 7.91	\$11.14	\$0.07
September	12.00	6.05	11.06	0.07
June	11.20	6.34	6.34	0.07
March	10.97	7.56	10.16	0.07
2007:				
December	\$10.16	\$ 6.15	\$ 7.29	\$0.07
September	11.06	8.62	9.50	0.07
June	13.64	10.99	10.99	0.07
March	13.52	9.08	13.26	0.07

First BanCorp has five outstanding series of non convertible preferred stock: 7.125% non-cumulative perpetual monthly income preferred stock, Series A (liquidation preference \$25 per share); 8.35% non-cumulative perpetual monthly income preferred stock, Series B (liquidation preference \$25 per share); 7.40% non-cumulative perpetual monthly income preferred stock, Series C (liquidation preference \$25 per share); 7.25% non-cumulative perpetual monthly income preferred stock, Series D (liquidation preference \$25 per share.); and 7.00% non-cumulative perpetual monthly income preferred stock, Series E (liquidation preference \$25 per share) (collectively Preferred Stock), which trade on the NYSE.

On January 16, 2009, the Corporation issued to the U.S. Treasury the Series F Preferred Stock and the Warrant, which transaction is described in Item 1 Recent Significant Events on page 9.

The Series A, B, C, D, E and F Preferred Stock rank on parity with respect to dividend rights and rights upon liquidation, winding up or dissolution. Holders of each series of preferred stock are entitled to receive cash dividends, when, as and if declared by the board of directors of First BanCorp out of funds legally available for dividends. The Purchase Agreement of the Series F Preferred stock contains limitations on 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), of common stock prior to October 14, 2008, which is \$0.07 per share.

The terms of the Corporation's preferred stock do not permit the Corporation to declare, set apart or pay any dividend or make any other distribution of assets on, or redeem, purchase, set apart or otherwise acquire shares of common stock or of any other class of stock of First BanCorp ranking junior to the preferred stock, unless all accrued and unpaid dividends on the preferred stock and any parity stock, for the twelve monthly dividend periods ending on the immediately preceding dividend payment date, shall have been paid or are paid contemporaneously;

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the full monthly dividend on the preferred stock and any parity stock for the then current month has been or is contemporaneously declared and paid or declared and set apart for payment; and the Corporation has not defaulted in the payment of the redemption price of any shares of the preferred stock and any parity stock called for redemption. If the Corporation is unable to pay in full the dividends on the preferred stock and on any other shares of stock of equal rank as to the payment of dividends, all dividends declared upon the preferred stock and any such other shares of stock will be declared pro rata.

The Corporation may not issue shares ranking, as to dividend rights or rights on liquidation, winding up and dissolution, senior to the Series A, B, C, D, E and F Preferred Stock, except with the consent of the holders of at least two-thirds of the outstanding aggregate liquidation preference of the Series A, B, C, D, E and F Preferred Stock.

Dividends

The Corporation has a policy of paying quarterly cash dividends on its outstanding shares of common stock subject to its earnings and financial condition. On July 30, 2009 after reporting a net loss for the quarter ended June 30, 2009, the Corporation announced that the Board of Directors resolved to suspend the payment of the common and preferred dividends (including the Series F Preferred Stock dividends), effective with the preferred dividend for the month of August 2009. During 2009, the Corporation declared a cash dividend of \$0.07 per share for the first two quarters of the year. During years 2008 and 2007, the Corporation declared a cash dividend of \$0.07 per share for each quarter of such years. The Corporation's ability to pay future dividends will necessarily depend upon its earnings and financial condition. See the discussion under Dividend Restrictions under Item 1 for additional information concerning restrictions on the payment of dividends that apply to the Corporation and FirstBank.

First BanCorp did not purchase any of its equity securities during 2009 or 2008.

The Puerto Rico Internal Revenue Code requires the withholding of income tax from dividend income derived by resident U.S. citizens, special partnerships, trusts and estates and non-resident U.S. citizens, custodians, partnerships, and corporations from sources within Puerto Rico.

Resident U.S. Citizens

A special tax of 10% is imposed on eligible dividends paid to individuals, special partnerships, trusts, and estates to be applied to all distributions unless the taxpayer specifically elects otherwise. Once this election is made it is irrevocable. However, the taxpayer can elect to include in gross income the eligible distributions received and take a credit for the amount of tax withheld. If the taxpayer does not make this election on the tax return, then he can exclude from gross income the distributions received and reported without claiming the credit for the tax withheld.

Nonresident U.S. Citizens

Nonresident U.S. citizens have the right to certain exemptions when a Withholding Tax Exemption Certificate (Form 2732) is properly completed and filed with the Corporation. The Corporation, as withholding agent, is authorized to withhold a tax of 10% only from the excess of the income paid over the applicable tax-exempt amount.

U.S. Corporations and Partnerships

Corporations and partnerships not organized under Puerto Rico laws that have not engaged in trade or business in Puerto Rico during the taxable year in which the dividend is paid are subject to the 10% dividend tax withholding. Corporations or partnerships not organized under the laws of Puerto Rico that have engaged in trade or business in Puerto Rico are not subject to the 10% withholding, but they must declare the dividend as gross income on their Puerto Rico income tax return.

Table of Contents***Securities authorized for issuance under equity compensation plans***

The following summarizes equity compensation plans approved by security holders and equity compensation plans that were not approved by security holders as of December 31, 2009:

Plan category	Number of Securities to be Issued Upon Exercise of Outstanding Options (A)	Weighted-Average Exercise Price of Outstanding Options, warrants and rights (B)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (A)) (C)
Equity compensation plans approved by stockholders	2,481,310 (1)	\$ 13.46	3,767,784 (2)
Equity compensation plans not approved by stockholders	N/A	N/A	N/A
Total	2,481,310	\$ 13.46	3,767,784

(1) Stock options granted under the 1997 stock option plan which expired on January 21, 2007. All outstanding awards under the stock option plan continue in full force and effect, subject to their original terms and the shares of common stock underlying the options are subject to adjustments for stock splits, reorganization

and other
similar events.

- (2) Securities available for future issuance under the First BanCorp 2008 Omnibus Incentive Plan (the Omnibus Plan) approved by stockholder on April 29, 2008. 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 3,800,000 shares of common stock, subject to adjustments for stock splits, reorganization and other similar events.

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STOCK PERFORMANCE GRAPH

The following Performance Graph shall not be deemed incorporated by reference by any general statement incorporating by reference this Annual Report on Form 10-K into any filing under the Securities Act of 1933, as amended (the Securities Act) or the Exchange Act, except to the extent that First BanCorp specifically incorporates this information by reference, and shall not otherwise be deemed filed under these Acts.

The graph below compares the cumulative total stockholder return of First BanCorp during the measurement period with the cumulative total return, assuming reinvestment of dividends, of the S&P 500 Index and the S&P Supercom Banks Index (the Peer Group). The Performance Graph assumes that \$100 was invested on December 31, 2004 in each of First BanCorp common stock, the S&P 500 Index and the Peer Group. The comparisons in this table are set forth in response to SEC disclosure requirements, and are therefore not intended to forecast or be indicative of future performance of First BanCorp s common stock.

The cumulative total stockholder return was obtained by dividing (i) the cumulative amount of dividends per share, assuming dividend reinvestment since the measurement point, December 31, 2004, plus (ii) the change in the per share price since the measurement date, by the share price at the measurement date.

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The following table sets forth certain selected consolidated financial data for each of the five years in the period ended December 31, 2009. This information should be read in conjunction with the audited consolidated financial statements and the related notes thereto.

SELECTED FINANCIAL DATA

(Dollars in thousands except for per share data and financial ratios results)

	Year Ended December 31,				
	2009	2008	2007	2006	2005
Condensed Income Statements:					
Total interest income	\$ 996,574	\$ 1,126,897	\$ 1,189,247	\$ 1,288,813	\$ 1,067,590
Total interest expense	477,532	599,016	738,231	845,119	635,271
Net interest income	519,042	527,881	451,016	443,694	432,319
Provision for loan and lease losses	579,858	190,948	120,610	74,991	50,644
Non-interest income	142,264	74,643	67,156	31,336	63,077
Non-interest expenses	352,101	333,371	307,843	287,963	315,132
(Loss) income before income taxes	(270,653)	78,205	89,719	112,076	129,620
Income tax (expense) benefit	(4,534)	31,732	(21,583)	(27,442)	(15,016)
Net (loss) income	(275,187)	109,937	68,136	84,634	114,604
Net (loss) income attributable to common stockholders	(322,075)	69,661	27,860	44,358	74,328
Per Common Share Results:					
Net (loss) income per common share basic	\$ (3.48)	\$ 0.75	\$ 0.32	\$ 0.54	\$ 0.92
Net (loss) income per common share diluted	\$ (3.48)	\$ 0.75	\$ 0.32	\$ 0.53	\$ 0.90
Cash dividends declared	\$ 0.14	\$ 0.28	\$ 0.28	\$ 0.28	\$ 0.28
Average shares outstanding	92,511	92,508	86,549	82,835	80,847
Average shares outstanding diluted	92,511	92,644	86,866	83,138	82,771
Book value per common share	\$ 7.25	\$ 10.78	\$ 9.42	\$ 8.16	\$ 8.01
Tangible book value per common share ⁽¹⁾	\$ 6.76	\$ 10.22	\$ 8.87	\$ 7.50	\$ 7.29
Balance Sheet Data:					
Loans and loans held for sale	\$ 13,949,226	\$ 13,088,292	\$ 11,799,746	\$ 11,263,980	\$ 12,685,929
Allowance for loan and lease losses	528,120	281,526	190,168	158,296	147,999
Money market and investment securities	4,866,617	5,709,154	4,811,413	5,544,183	6,653,924
Intangible Assets	44,698	52,083	51,034	54,908	58,292
Deferred tax asset, net	109,197	128,039	90,130	162,096	130,140
Total assets	19,628,448	19,491,268	17,186,931	17,390,256	19,917,651
Deposits	12,669,047	13,057,430	11,034,521	11,004,287	12,463,752
Borrowings	5,214,147	4,736,670	4,460,006	4,662,271	5,750,197
Total preferred equity	928,508	550,100	550,100	550,100	550,100
Total common equity	644,062	940,628	896,810	709,620	663,416
Accumulated other comprehensive income (loss), net of tax	26,493	57,389	(25,264)	(30,167)	(15,675)
Total equity	1,599,063	1,548,117	1,421,646	1,229,553	1,197,841
Selected Financial Ratios (In Percent):					
Profitability:					
Return on Average Assets	(1.39)	0.59	0.40	0.44	0.64

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Return on Average Total Equity	(14.84)	7.67	5.14	7.06	8.98
Return on Average Common Equity	(34.07)	7.89	3.59	6.85	10.23
Average Total Equity to Average Total Assets	9.36	7.74	7.70	6.25	7.09
Interest Rate Spread ⁽¹⁾⁽²⁾	2.62	2.83	2.29	2.35	2.87
Interest Rate Margin ⁽¹⁾⁽²⁾	2.93	3.20	2.83	2.84	3.23
Tangible common equity ratio ⁽¹⁾	3.20	4.87	4.79	3.60	2.97
Dividend payout ratio	(4.03)	37.19	88.32	52.50	30.46
Efficiency ratio ⁽³⁾	53.24	55.33	59.41	60.62	63.61

Asset Quality:

Allowance for loan and lease losses to loans receivable	3.79	2.15	1.61	1.41	1.17
Net charge-offs to average loans	2.48	0.87	0.79	0.55	0.39
Provision for loan and lease losses to net charge-offs	1.74x	1.76x	1.36x	1.16x	1.12x
Non-performing assets to total assets	8.71	3.27	2.56	1.54	0.75
Non-performing loans to total loans receivable	11.23	4.49	3.50	2.24	1.06
Allowance to total non-performing loans	33.77	47.95	46.04	62.79	110.18
Allowance to total non-performing loans, excluding residential real estate loans	47.06	90.16	93.23	115.33	186.06

Other Information:

Common Stock Price: End of period	\$ 2.30	\$ 11.14	\$ 7.29	\$ 9.53	\$ 12.41
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(1) Non-gaap measures. Refer to Capital discussion below for additional information of the components and reconciliation of these measures.

(2) On a tax equivalent basis (see Net Interest Income discussion below).

(3) Non-interest expenses 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.

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

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

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), Grupo Empresas de Servicios Financieros (d/b/a PR Finance Group) 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.

OVERVIEW OF RESULTS OF OPERATIONS

First BanCorp's results of operations 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 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 year ended December 31, 2009, non-interest expenses (such as personnel, occupancy and other costs), non-interest income (mainly service charges and fees on loans and deposits and insurance income), the results of its hedging activities, gains (losses) on investments, gains (losses) on mortgage banking activities, and income taxes which also significantly affected 2009 results.

Net loss for the year ended December 31, 2009 amounted to \$275.2 million or \$(3.48) per diluted common share, compared to net income of \$109.9 million or \$0.75 per diluted common share for 2008 and net income of \$68.1 million or \$0.32 per diluted common share for 2007.

The Corporation's financial results for 2009, as compared to 2008, were principally impacted by: (i) an increase of \$388.9 million in the provision for loan and lease losses attributable to the significant increase in the volume of non-performing and impaired loans, the migration of loans to higher risk categories, increases in loss factors used to determine general reserves to account for increases in charge-offs, delinquency levels and weak economic conditions, and the overall growth of the loan portfolio, (ii) an increase of \$36.3 million in income tax expense, affected by a non-cash increase of \$184.4 million in the Corporation's deferred tax asset valuation allowance due to losses incurred in 2009, (iii) an increase of \$18.7 million in non-interest expenses driven by increases in the FDIC deposit insurance premium partially offset by a reduction in employees' compensation and benefit expenses, and (iv) a decrease of \$8.8 million in net interest income mainly due to lower loan yields adversely affected by the higher volume of non-performing loans and the repricing of adjustable rate commercial and construction loans tied to short-term indexes. These factors were partially offset by an increase of \$67.6 million in non-interest income primarily due to realized gains of \$86.8 million on the sale of investment securities in 2009, mainly U.S. Agency mortgage-backed securities.

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The following table summarizes the effect of the aforementioned factors and other factors that significantly impacted financial results in previous years on net (loss) income attributable to common stockholders and (loss) earnings per common share for the last three years:

	Year Ended December 31,					
	2009		2008		2007	
	Dollars	Per Share	Dollars	Per Share	Dollars	Per Share
	(In thousands, except for per common share amounts)					
Net income attributable to common stockholders for prior year	\$ 69,661	\$ 0.75	\$ 27,860	\$ 0.32	\$ 44,358	\$ 0.53
Increase (decrease) from changes in:						
Net interest income	(8,839)	(0.10)	76,865	0.88	7,322	0.09
Provision for loan and lease losses	(388,910)	(4.20)	(70,338)	(0.81)	(45,619)	(0.55)
Net gain (loss) on investments and impairments	63,953	0.69	23,919	0.28	5,468	0.06
Gain (loss) on partial extinguishment and recharacterization of secured commercial loans to local financial institutions			(2,497)	(0.03)	13,137	0.16
Gain on sale of credit card portfolio			(2,819)	(0.03)	2,319	0.03
Insurance reimbursement and other agreements related to a contingency settlement			(15,075)	(0.17)	15,075	0.18
Other non-interest income	3,668	0.04	3,959	0.05	(179)	
Employees compensation and benefits	9,119	0.10	(1,490)	(0.02)	(12,840)	(0.15)
Professional fees	592	0.01	4,942	0.06	11,344	0.13
Deposit insurance premium	(30,471)	(0.33)	(3,424)	(0.04)	(5,073)	(0.06)
Net loss on REO operations	(490)	(0.01)	(18,973)	(0.22)	(2,382)	(0.03)
Core deposit intangible impairment	(3,988)	(0.04)				
All other operating expenses	6,508	0.07	(6,583)	(0.08)	(10,929)	(0.13)
Income tax provision	(36,266)	(0.39)	53,315	0.61	5,859	0.07
Net (loss) income before changes in preferred stock dividends, preferred	(315,463)	(3.41)	69,661	0.80	27,860	0.33

discount amortization and change in average common shares							
Change in preferred dividends and preferred discount amortization	(6,612)	(0.07)					
Change in average common shares (1)				(0.05)			(0.01)
Net (loss) income attributable to common stockholders	\$ (322,075)	\$ (3.48)	\$ 69,661	\$ 0.75	\$ 27,860	\$ 0.32	

(1) For 2008, mainly attributed to the sale of 9.250 million common shares to the Bank of Nova Scotia (Scotiabank) in the second half of 2007.

Net loss for the year ended December 31, 2009 was \$275.2 million compared to net income of \$109.9 million and net income of \$68.1 million for the years ended December 31, 2008 and 2007, respectively.

Diluted loss per common share for the year ended December 31, 2009 amounted to \$(3.48) compared to earnings per diluted share of \$0.75 and \$0.32 for the years ended December 31, 2008 and 2007, respectively.

Net interest income for the year ended December 31, 2009 was \$519.0 million compared to \$527.9 million and \$451.0 million for the years ended December 31, 2008 and 2007, respectively. Net interest spread and margin on an adjusted tax equivalent basis (for definition and reconciliation of this non-GAAP measure, refer to the *Net Interest Income* discussion below) were 2.62% and 2.93%, respectively, down 21 and 27 basis points from 2008. The decrease for 2009 compared to 2008 was mainly associated with a significant increase in non-performing loans and the repricing of floating-rate commercial and construction loans at lower rates due to decreases in market interest rates such as three-month LIBOR and the Prime rate, even though the Corporation is actively increasing spreads on loan renewals. The Corporation increased the use of interest rate floors in new commercial and construction loans agreements and renewals in 2009 to protect net interest margins going forward. Lower loan yields more than offset the benefit of lower short-term rates in the average cost of funding and the increase in average interest-earning assets. Refer to the *Net Interest Income* discussion below for additional information.

The increase in net interest income for 2008, compared to 2007, was mainly associated with a decrease in the average cost of funds resulting from lower short-term interest rates and, to a lesser extent, a higher volume of interest-earning assets. The decrease in funding costs more than offset lower loans yields resulting from the repricing of variable-rate construction and commercial loans tied to short-term indexes and from a higher volume of non-accrual loans.

The provision for loan and lease losses for 2009 was \$579.9 million compared to \$190.9 million and \$120.6 million for 2008 and 2007, respectively. The increase for 2009, as compared to 2008, was mainly attributable

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to the significant increase in non-performing loans and increases in specific reserves for impaired commercial and construction loans. Also, the migration of loans to higher risk categories and increases to loss factors used to determine the general reserve allowance contributed to the higher provision.

The increase for 2008, as compared to 2007, was mainly attributable to the significant increase in delinquency levels and increases in specific reserves for impaired commercial and construction loans. During 2008, the Corporation experienced continued stress in the credit quality of and worsening trends on its construction loan portfolio, in particular, condo-conversion loans affected by the continuing deterioration in the health of the economy, an oversupply of new homes and declining housing prices in the United States and on its commercial loan portfolio which was adversely impacted by deteriorating economic conditions in Puerto Rico. Also, higher reserves for residential mortgage loans in Puerto Rico and in the United States were necessary to account for the credit risk tied to recessionary conditions in the economy.

Refer to the Provision for Loan and Lease Losses and Risk Management discussions below for additional information and further analysis of the allowance for loan and lease losses and non-performing assets and related ratios.

Non-interest income for the year ended December 31, 2009 was \$142.3 million compared to \$74.6 million and \$67.2 million for the years ended December 31, 2008 and 2007, respectively. The increase in non-interest income in 2009, compared to 2008, was mainly related to a \$59.6 million increase in realized gains on the sale of investment securities, primarily reflecting a \$79.9 million gain on the sale of mortgage-backed securities (MBS) (mainly U.S. agency fixed-rate MBS), compared to realized gains on the sale of MBS of \$17.7 million in 2008. In an effort to manage interest rate risk, and taking advantage of favorable market valuations, approximately \$1.8 billion of U.S. agency MBS (mainly 30 year fixed-rate U.S. agency MBS) were sold in 2009, compared to approximately \$526 million of U.S. agency MBS sold in 2008. Also contributing to higher non-interest income was the \$5.3 million increase in gains from mortgage banking activities, due to the increased volume of loan sales and securitizations. Servicing assets recorded at the time of sale amounted to \$6.1 million for 2009 compared to \$1.6 million for 2008. The increase was mainly related to \$4.6 million of capitalized servicing assets in connection with the securitization of approximately \$305 million FHA/VA mortgage loans into GNMA MBS. For the first time in several years, the Corporation has been engaged in the securitization of mortgage loans since early 2009.

The increase in non-interest income in 2008, compared to 2007, was related to a realized gain of \$17.7 million on the sale of investment securities (mainly U.S. sponsored agency fixed-rate MBS) and to the gain of \$9.3 million on the sale of part of the Corporation's investment in VISA in connection with VISA's initial public offering (IPO). A surge in MBS prices, mainly due to announcements of the Federal Reserve (FED) that it will invest up to \$600 billion in obligations from U.S. government-sponsored agencies, including \$500 billion in MBS, provided an opportunity to realize a sale of approximately \$284 million fixed-rate U.S. agency MBS at a gain of \$11.0 million. Early in 2008, a spike and subsequent contraction in yield spread for U.S. agency MBS also provided an opportunity for the sale of approximately \$242 million and a realized gain of \$6.9 million. Higher point of sale (POS) and ATM interchange fee income and an increase in fee income from cash management services provided to corporate customers also contributed to the increase in non-interest income. The increase in non-interest income attributable to these activities was partially offset, when comparing 2008 to 2007, by isolated events such as the \$15.1 million income recognition for reimbursement of expenses, mainly from insurance carriers, related to the class action lawsuit settled in 2007, and a gain of \$2.8 million on the sale of a credit card portfolio and of \$2.5 million on the partial extinguishment and recharacterization of a secured commercial loan to a local financial institution that were all recognized in 2007.

Refer to Non-Interest Income discussion below for additional information.

Non-interest expenses for 2009 was \$352.1 million compared to \$333.4 million and \$307.8 million for 2008 and 2007, respectively. The increase in non-interest expenses for 2009, as compared to 2008, was principally attributable to: (i) an increase of \$30.5 million in the FDIC deposit insurance premium, including \$8.9 million for the special assessment levied by the FDIC in 2009 and increases in regular assessment rates, (ii) a \$4.0 million core deposit intangible impairment charge, and (iii) a \$1.8 million increase in the reserve for probable losses on outstanding unfunded loan commitments. The aforementioned increases were partially offset by decreases in

certain controllable expenses such as: (i) a \$9.1 million decrease in employees' compensation and benefit expenses, due to a lower headcount and reductions in bonuses, incentive compensation and overtime costs, (ii) a \$3.4 million decrease in business promotion expenses due to a lower

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level of marketing activities, and (iii) a \$1.1 million decrease in taxes, other than income taxes, driven by a reduction in municipal taxes which are assessed based on taxable gross revenues.

The increase in non-interest expenses for 2008, as compared to 2007, was principally attributable to: (i) a higher net loss on REO operations that increased to \$21.4 million for 2008 from \$2.4 million for 2007, driven by a higher inventory of repossessed properties and declining real estate prices, mainly in the U.S. mainland, that have caused write-downs on the value of repossessed properties, and (ii) an increase of \$3.4 million in deposit insurance premium expense, as the Corporation used available one-time credits to offset the premium increase in 2007 resulting from a new assessment system adopted by the FDIC, and (iii) higher occupancy and equipment expenses, an increase of \$2.9 million tied to the growth of the Corporation's operations. The Corporation was able to continue the growth of its operations without incurring substantial additional non-interest expenses as reflected by a slight increase of 2% in non-interest expenses, excluding the increase in REO operations losses. Modest increases were observed in occupancy and equipment expenses, an increase of \$2.9 million, and in employees compensation and benefit, an increase of \$1.5 million. Refer to Non-Interest Expenses discussion below for additional information.

For 2009, the Corporation recorded an income tax expense of \$4.5 million, compared to an income tax benefit of \$31.7 million for 2008. The income tax expense for 2009 mainly resulted from the aforementioned \$184.4 million non-cash increase in the valuation allowance for the Corporation's deferred tax asset. The increase in the valuation allowance was driven by the losses incurred in 2009 that placed FirstBank in a three-year cumulative loss position as of the end of the third quarter of 2009.

For 2008, the Corporation recorded an income tax benefit of \$31.7 million, compared to an income tax expense of \$21.6 million for 2007. The fluctuation was mainly related to lower taxable income. A significant portion of revenues was derived from tax-exempt assets and operations conducted through the international banking entity, FirstBank Overseas Corporation. Also, the positive fluctuation in financial results was impacted by two transactions: (i) a reversal of \$10.6 million of Unrecognized Tax Benefits (UTBs) during the second quarter of 2008 for positions taken on income tax returns due to the lapse of the statute of limitations for the 2003 taxable year, and (ii) the recognition of an income tax benefit of \$5.4 million in connection with an agreement entered into with the Puerto Rico Department of Treasury during the first quarter of 2008 that established a multi-year allocation schedule for deductibility of the \$74.25 million payment made by the Corporation during 2007 to settle a securities class action suit.

Refer to Income Taxes discussion below for additional information.

Total assets as of December 31, 2009 amounted to \$19.6 billion, an increase of \$137.2 million compared to \$19.5 billion as of December 31, 2008. The Corporation's loan portfolio increased by \$860.9 million (before the allowance for loan and lease losses), driven by new originations, mainly credit facilities extended to the Puerto Rico Government and/or its political subdivisions. Also, an increase of \$298.4 million in cash and cash equivalents contributed to the increase in total assets, as the Corporation improved its liquidity position as a precautionary measure given current volatile market conditions. Partially offsetting the increase in loans and liquid assets was a \$790.8 million decrease in investment securities, driven by sales and principal repayments of MBS.

As of December 31, 2009, total liabilities amounted to \$18.0 billion, an increase of \$86.2 million as compared to \$17.9 billion as of December 31, 2008. The increase in total liabilities was mainly attributable to an increase of \$818 million in short-term advances from the FED and FHLB and an increase of \$480 million in non-brokered deposits, partially offset by a decrease of \$868.4 million in brokered CDs and a decrease of \$344.4 million in repurchase agreements. The Corporation has been reducing the reliance on brokered CDs and is focused on core deposit growth initiatives in all of the markets served.

The Corporation's stockholders' equity amounted to \$1.6 billion as of December 31, 2009, an increase of \$50.9 million compared to the balance as of December 31, 2008, driven by the \$400 million investment by the United States Department of the Treasury (the U.S. Treasury) in preferred stock of the Corporation through the U.S. Treasury Troubled Asset Relief Program (TARP) Capital Purchase Program. This was partially offset by the net loss of \$275.2 million recorded for 2009, dividends paid amounting to \$43.1 million in 2009 (\$13.0 million on common stock, or \$0.14 per share, and \$30.1 million on preferred stock) and a \$30.9 million decrease in other

comprehensive income mainly due to a noncredit-related impairment of

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\$31.7 million on private label MBS.

Total loan production, including purchases and refinancings, for the year ended December 31, 2009 was \$4.8 billion compared to \$4.2 billion and \$4.1 billion for the years ended December 31, 2008 and 2007, respectively. The increase in loan production in 2009, as compared to 2008, was mainly associated with a \$977.9 million increase in commercial loan originations driven by approximately \$1.7 billion in credit facilities extended to the Puerto Rico Government and/or its political subdivisions. Partially offsetting the increase in the originations of commercial loans was a decrease of \$303.3 million in originations of consumer loans and of \$98.5 million in residential mortgage loan originations adversely affected by weak economic conditions in Puerto Rico. The increase in loan production in 2008, as compared to 2007, was mainly associated with an increase in commercial loan originations and the purchase of a \$218 million auto loan portfolio.

Total non-performing assets as of December 31, 2009 was \$1.71 billion compared to \$637.2 million as of December 31, 2008. Even though deterioration in credit quality was observed in all of the Corporation's portfolios, it was more significant in the construction and commercial loan portfolios, which were affected by both the stagnant housing market and further weakening in the economies of the markets served during most of 2009. The increase in non-performing assets was led by an increase of \$518.0 million in non-performing construction loans, of which \$314.1 million is related to the construction loan portfolio in the Puerto Rico portfolio and \$205.2 million is related to construction projects in Florida. Other portfolios that experienced a significant growth in credit risk, mainly in Puerto Rico, include: (i) a \$183.0 million increase in non-performing commercial and industrial (C&I) loans, (ii) a \$166.7 million increase in non-performing residential mortgage loans, and (iii) a \$110.6 million increase in non-performing commercial mortgage loans. Also, during 2009, the Corporation classified as non-performing investment securities with a book value of \$64.5 million that were pledged to Lehman Brothers Special Financing, Inc., in connection with several interest rate swap agreements entered into with that institution. Considering that the investment securities have not yet been recovered by the Corporation, despite its efforts, the Corporation decided to classify such investments as non-performing. Refer to the Risk Management Non-accruing and Non-performing Assets section below for additional information with respect to non-performing assets by geographic areas and recent actions taken by the Corporation to reduce its exposure to troubled loans.

Table of Contents**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; 6) derivative financial instruments; and 7) income recognition on loans. These critical accounting policies involve judgments, estimates and assumptions made by management that affect the recorded assets and liabilities and contingent assets and liabilities disclosed 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.

Allowance for Loan and Lease Losses

The Corporation maintains the allowance for loan and lease losses at a level considered adequate to absorb losses currently inherent in the loan and lease portfolio. 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

A specific valuation allowance is established for those commercial and real estate loans classified as impaired, primarily when the collateral value of the loan (if the impaired loan is determined to be collateral dependent) or the present value of the expected future cash flows discounted at the loan s effective rate is lower than the carrying amount of that loan. To compute the specific valuation allowance, commercial and real estate, including residential mortgage loans with a principal balance of \$1 million or more are evaluated individually as well as smaller residential mortgage loans considered impaired based on their high delinquency and loan-to-value levels. When foreclosure is probable, the impairment is measured based on the fair value of the collateral. The fair value of the collateral is generally obtained from appraisals. Updated appraisals are obtained when the Corporation determines that loans are impaired and are updated annually thereafter. In addition, appraisals are also obtained for certain residential mortgage loans on a spot basis based on specific characteristics such as delinquency levels, age of the appraisal, and loan-to-value ratios. Deficiencies from the excess of the recorded investment in collateral dependent loans over the resulting fair value of the collateral are charged-off when deemed uncollectible.

For all other loans, which include, small, homogeneous loans, such as auto loans, consumer loans, finance lease loans, residential mortgages, and commercial and construction loans not considered impaired or in amounts under \$1 million, the Corporation maintains a general valuation allowance. The methodology to compute the general valuation allowance has not change in the past 2 years. The Corporation updates the factors used to compute the reserve factors on a quarterly basis. The general reserve is primarily determined by applying loss factors according to the loan type and assigned risk category (pass, special mention and substandard not impaired; all doubtful loans are considered impaired). The general reserve for consumer loans is based on factors such as delinquency trends, credit bureau score bands, portfolio type, geographical location, bankruptcy trends, recent market transactions, and other environmental factors such as economic forecasts. The analysis of the residential mortgage pools are performed at the individual loan level and then aggregated to determine the expected loss ratio. The model applies risk-adjusted prepayment curves, default curves, and severity curves to each loan in the pool. The severity is affected by the expected house price scenario based on recent house price trends. Default curves are used in the model to determine expected delinquency levels. The risk-adjusted timing of liquidation and associated costs are used in the model and are risk-adjusted for the area in which the property is located (Puerto Rico, Florida, or Virgin Islands). For commercial loans, including construction loans, the general reserve is based on historical loss ratios, trends in non-accrual loans, loan type, risk-rating, geographical location, changes in collateral values for collateral dependent loans and gross product or unemployment data for the geographical region. The methodology of accounting for all probable losses in loans not individually measured for impairment purposes is made in accordance with authoritative accounting guidance that requires losses be accrued when they are probable of occurring and estimable.

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The blended general reserve factors utilized for all portfolios increased during 2009 due to the continued deterioration in the economy and the continued increase in delinquencies, charge-offs, home values and most other economic indicators utilized. The blended general reserve factor for residential mortgage loans increased from 0.43% in 2008 to 0.91% in 2009. For commercial mortgage loans the blended general reserve factor increased from 0.62% in 2008 to 2.41% in 2009. For C&I loans the blended general reserve factor increased from 1.31% in 2008 to 2.44% in 2009. The construction loans blended general factor increased from 2.18% in 2008 to 9.82% in 2009. The consumer and finance leases reserve factor increased from 4.31% in 2008 to 4.36% in 2009.

Other-than-temporary impairments

On a quarterly basis, the Corporation performs an assessment to determine whether there have been any events or circumstances indicating that a security with an unrealized loss has suffered an other-than-temporary impairment (OTTI). A security is considered impaired if the fair value is less than its amortized cost basis.

The Corporation evaluates if the impairment is other-than-temporary depending upon whether the portfolio is of fixed income securities or equity securities as further described below. The Corporation employs a systematic methodology that considers all available evidence in evaluating a potential impairment of its investments.

The impairment analysis of fixed income securities places special emphasis on the analysis of the cash position of the issuer and its cash and capital generation capacity, which could increase or diminish the issuer's ability to repay its bond obligations, the length of time and the extent to which the fair value has been less than the amortized cost basis and changes in the near-term prospects of the underlying collateral, if applicable, such as changes in default rates, loss severity given default and significant changes in prepayment assumptions. In light of current volatile economic and financial market conditions, the Corporation also takes 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. In April 2009, the Financial Accounting Standard Board (FASB) amended the OTTI model for debt securities. OTTI losses are recognized in earnings if the Corporation 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 the Corporation does not expect to sell a debt security, expected cash flows to be received are evaluated to 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 is recorded as a component of Net impairment losses on investment securities in the statements of (loss) income, while the remaining portion of the impairment loss is recognized in other comprehensive income, net of taxes. The previous amortized cost basis less the OTTI recognized in earnings is the new amortized cost basis of the investment. The new amortized cost basis is not adjusted for subsequent recoveries in fair value. However, for debt securities for which OTTI was recognized in earnings, the difference between the new amortized cost basis and the cash flows expected to be collected is accreted as interest income.

Prior to April 1, 2009, an unrealized loss was considered other-than-temporary and recorded in earnings if (i) it was probable that the holder would not collect all amounts due according to contractual terms of the debt security, or (ii) the fair value was below the amortized cost of the 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.

The impairment model for equity securities was not affected by the aforementioned FASB amendment. The impairment analysis of equity securities is performed and reviewed on an ongoing basis based on the latest financial information and any supporting research report made by a major brokerage firm. This analysis is very subjective and based, among other things, on relevant financial data such as capitalization, cash flow, liquidity, systematic risk, and debt outstanding of the issuer. Management also considers the issuer's industry trends, the historical performance of the stock, credit ratings as well as the Corporation's intent to hold the security for an extended period. If management believes there is a low probability of recovering book value in a reasonable time frame, then an impairment will be recorded by writing the security down to market value. As previously mentioned, equity securities are monitored on an ongoing basis but special attention is given to those securities that have experienced a decline in fair value for six months or more. An impairment charge is generally recognized when the fair value of an equity security has remained significantly below cost for a period of twelve consecutive months or more.

Table of Contents**Income Taxes**

The Corporation is required to estimate income taxes in preparing its consolidated financial statements. This involves the estimation of current income tax expense together with an assessment of temporary differences resulting from differences in the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The determination of current income tax expense involves estimates and assumptions that require the Corporation to assume certain positions based on its interpretation of current tax regulations. Management assesses the relative benefits 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. Changes in assumptions affecting estimates may be required in the future and estimated tax liabilities may need to be increased or decreased accordingly. The accrual of tax contingencies is adjusted in light of changing facts and circumstances, such as the progress of tax audits, case law and emerging legislation. The Corporation's effective tax rate includes the impact of tax contingencies and changes to such accruals, as considered appropriate by management. When particular matters arise, a number of years may elapse before such matters are audited by the taxing authorities and finally resolved. Favorable resolution of such matters or the expiration of the statute of limitations may result in the release of tax contingencies which are recognized as a reduction to the Corporation's effective rate in the year of resolution. Unfavorable settlement of any particular issue could increase the effective rate and may require the use of cash in the year of resolution. As of December 31, 2009, there were no open income tax investigations. Information regarding income taxes is included in Note 27 to the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K.

The determination of deferred tax expense or benefit is based on changes in the carrying amounts of assets and liabilities that generate temporary differences. The carrying value of the Corporation's net deferred tax assets assumes that the Corporation will be able to generate sufficient future taxable income based on estimates and assumptions. If these estimates and related assumptions change, the Corporation may be required to record valuation allowances against its deferred tax assets resulting in additional income tax expense in the consolidated statements of income. Management evaluates its deferred tax assets on a quarterly basis and assesses the need for a valuation allowance, if any. A valuation allowance is established when management believes that it is more likely than not that some portion of its deferred tax assets will not be realized. Changes in valuation allowance from period to period are included in the Corporation's tax provision in the period of change (see Note 27 to the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K).

Accounting for Income Taxes requires companies to make adjustments to their financial statements in the quarter that new tax legislation is enacted. 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 capital gain statutory tax rate from 15% to 15.75%. This temporary measure is effective for tax years that commenced after December 31, 2008 and before January 1, 2012. Also, under the Act, all IBEs 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 commence after December 31, 2008 and before January 1, 2012. The effect of a higher temporary statutory tax rate over the normal statutory tax rate resulted in an additional income tax benefit of \$10.4 million for 2009 that was partially offset by an income tax provision of \$6.6 million related to the special 5% tax on the operations FirstBank Overseas Corporation. For 2007 and 2008, the maximum marginal corporate income tax rate was 39%.

The FASB issued authoritative guidance that 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 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 Unrecognized

Tax Benefit (UTB). The Corporation classifies interest and penalties, if any, related to UTBs as
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components of income tax expense. Refer to Note 27 of the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K for required disclosures and further information related to this accounting guidance.

Table of Contents**Investment Securities Classification and Related Values**

Management determines the appropriate classification of debt and equity securities at the time of purchase. Debt securities are classified as held-to-maturity when the Corporation has the intent and ability to hold the securities to maturity. Held-to-maturity (HTM) securities are stated at amortized cost. Debt and equity securities are classified as trading when the Corporation has the intent to sell the securities in the near term. Debt and equity securities classified as trading securities are reported at fair value, with unrealized gains and losses included in earnings. Debt and equity securities not classified as HTM or trading, except for equity securities that do not have readily available fair values, are classified as available-for-sale (AFS). AFS securities are reported at fair value, with unrealized gains and losses excluded from earnings and reported net of deferred taxes in accumulated other comprehensive income (a component of stockholders' equity) and do not affect earnings until realized or are deemed to be other-than-temporarily impaired. Investments in equity securities that do not have publicly and readily determinable fair values are classified as other equity securities in the statement of financial condition and carried at the lower of cost or realizable value. The determination of fair value applies to certain of the Corporation's assets and liabilities, including the investment portfolio. Fair values are volatile and are affected by factors such as market interest rates, prepayment speeds and discount rates.

Valuation of financial instruments

The measurement of fair value is fundamental to the Corporation's presentation of its financial condition and results of operations. The Corporation holds fixed income and equity securities, derivatives, investments and other financial instruments at fair value. The Corporation holds its investments and liabilities on the statement of financial condition mainly to manage liquidity needs and interest rate risks. A substantial part of these assets and liabilities is reflected at fair value on the Corporation's financial statements.

The Corporation adopted authoritative guidance issued by the FASB for fair value measurements which 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 that 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** Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- Level 2** Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; 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 3** Valuations are observed from unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The following is a description of the valuation methodologies used for instruments measured at fair value:

Callable Brokered CDs (Level 2 inputs)

The fair value of callable brokered CDs, which are included within deposits and elected to be measured at fair value, is determined using discounted cash flow analyses over the full term of the CDs. The valuation uses a Hull-White Interest Rate Tree approach for the CDs with callable option components, an industry-standard approach for valuing instruments with interest rate call options. The model assumes that the embedded options are exercised economically. 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 and value the cancellation option in the deposits. The fair value does not incorporate the risk of nonperformance, since the callable brokered

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CDs are participated out by brokers in shares of less than \$100,000 and insured by the FDIC. As of December 31, 2009, there were no callable brokered CDs outstanding measured at fair value since they were all called during 2009.

Medium-Term Notes (Level 2 inputs)

The fair value of medium-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.

Investment Securities

The fair value of investment securities is the market value based on quoted market prices, when available, or market prices for identical or comparable assets 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 (Level 3), as is the case with certain private label mortgage-backed securities held by the Corporation. Unlike U.S. agency mortgage-backed securities, the fair value of these private label securities cannot be readily determined because they are not actively traded in securities markets. Significant inputs used for fair value determination consist of specific characteristics such as information used in the prepayment model, which follows the amortizing schedule of the underlying loans, which is an unobservable input.

Private label mortgage-backed securities are collateralized by fixed-rate mortgages on single-family residential properties in the United States and the interest rate is variable, tied to 3-month LIBOR and limited to the weighted-average coupon of the underlying collateral. The market valuation is derived from a model and 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 non-rated security and 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 of the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K for additional information.

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 counterparts when appropriate, except when collateral is pledged. That is, on interest rate swaps, the credit risk of both counterparts 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 and, prior to June 30, 2009, included interest rate swaps to economically hedge brokered CDs and medium-term notes. For these interest rate swaps, a credit component is not considered in the valuation since the

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Corporation fully collateralizes with investment securities any mark-to-market loss with the counterparty and, if there are market gains, the counterparty must deliver collateral to the Corporation.

Certain derivatives with limited market activity, as is the case with derivative instruments named as reference caps, are valued using models that consider unobservable market parameters (Level 3). Reference caps are used mainly to hedge interest rate risk inherent in private label mortgage-backed securities, thus are tied to the notional amount of the underlying fixed-rate mortgage loans originated in the United States. Significant inputs used for fair value determination consist of specific characteristics such as information used in the prepayment model which follows the amortizing schedule of the underlying loans, which is an unobservable input. The valuation model uses the Black formula, which is a benchmark standard in the financial industry. The Black formula is similar to the Black-Scholes formula for valuing stock options except that the spot price of the underlying is replaced by the forward price. The Black formula uses as inputs the strike price of the cap, forward LIBOR rates, volatility estimates and discount rates to estimate the option value. LIBOR rates and swap rates are obtained from Bloomberg L.P. (Bloomberg) every day and build zero coupon curve based on the Bloomberg LIBOR/Swap curve. The discount factor is then calculated from the zero coupon curve. The cap is the sum of all caplets. For each caplet, the rate is reset at the beginning of each reporting period and payments are made at the end of each period. The cash flow of caplet is then discounted from each payment date.

Derivative Financial Instruments

As part of the Corporation's overall interest rate risk management, the Corporation utilizes derivative instruments, including interest rate swaps, interest rate caps and options to manage interest rate risk. All derivative instruments are measured and recognized on the Consolidated Statements of Financial Condition at their fair value. On the date the derivative instrument contract is entered into, the Corporation may designate the derivative as (1) a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment (fair value hedge), (2) a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge) or (3) as a standalone derivative instrument, including economic hedges that the Corporation has not formally documented as a fair value or cash flow hedge. Changes in the fair value of a derivative instrument that is highly effective and that is designated and qualifies as a fair-value hedge, along with changes in the fair value of the hedged asset or liability that is attributable to the hedged risk (including gains or losses on firm commitments), are recorded in current-period earnings as interest income or interest expense depending upon whether an asset or liability is being hedged. Similarly, the changes in the fair value of standalone derivative instruments or derivatives not qualifying or designated for hedge accounting are reported in current-period earnings as interest income or interest expense depending upon whether an asset or liability is being economically hedged. Changes in the fair value of a derivative instrument that is highly effective and that is designated and qualifies as a cash-flow hedge, if any, are recorded in other comprehensive income in the stockholders' equity section of the Consolidated Statements of Financial Condition until earnings are affected by the variability of cash flows (e.g., when periodic settlements on a variable-rate asset or liability are recorded in earnings). As of December 31, 2009 and 2008, all derivatives held by the Corporation were considered economic undesignated hedges recorded at fair value with the resulting gain or loss recognized in current period earnings.

Prior to entering into an accounting hedge transaction or designating a hedge, the Corporation formally documents the relationship between the hedging instrument and the hedged item, as well as the risk management objective and strategy for undertaking the hedge transaction. This process includes linking all derivative instruments that are designated as fair value or cash flow hedges, if any, to specific assets and liabilities on the statements of financial condition or to specific firm commitments or forecasted transactions along with a formal assessment at both inception of the hedge and on an ongoing basis as to the effectiveness of the derivative instrument in offsetting changes in fair values or cash flows of the hedged item. The Corporation discontinues hedge accounting prospectively when it determines that the derivative is not effective or will no longer be effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative expires, is sold, or terminated, or management determines that designation of the derivative as a hedging instrument is no longer appropriate. When a fair value hedge is discontinued, the hedged asset or liability is no longer adjusted for changes in fair value and the existing basis adjustment is amortized or accreted over the remaining life of the asset or liability as a yield adjustment.

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The Corporation occasionally purchases or originates financial instruments that contain embedded derivatives. At inception of the financial instrument, the Corporation assesses: (1) if the economic characteristics of the embedded derivative are clearly and closely related to the economic characteristics of the financial instrument (host contract), (2) if the financial instrument that embodies both the embedded derivative and the host contract is measured at fair value with changes in fair value reported in earnings, or (3) if a separate instrument with the same terms as the embedded instrument would not meet the definition of a derivative. If the embedded derivative does not meet any of these conditions, it is separated from the host contract and carried at fair value with changes recorded in current period earnings as part of net interest income.

Effective January 1, 2007, the Corporation elected to early adopt authoritative guidance issued by the FASB that allows entities to choose to measure certain financial assets and liabilities at fair value with any changes in fair value reflected in earnings. The Corporation adopted the fair value option for callable fixed-rate medium-term notes and callable brokered certificates of deposit that were hedged with interest rate swaps. One of the main considerations in the determination to adopt the fair value option for these instruments was to eliminate the operational procedures required by the long-haul method of accounting in terms of documentation, effectiveness assessment, and manual procedures followed by the Corporation to fulfill the requirements specified by authoritative guidance issued by the FASB for derivative instruments designated as fair value hedges.

With the Corporation's elimination of the use of the long-haul method in connection with the adoption of the fair value option, the Corporation no longer amortizes or accretes the basis adjustment for the financial liabilities elected to be measured at fair value. The basis adjustment amortization or accretion is the reversal of the basis differential between the market value and book value recognized at the inception of fair value hedge accounting as well as the change in value of the hedged brokered CDs and medium-term notes recognized since the implementation of the long-haul method. Since the time the Corporation implemented the long-haul method, it had recognized changes in the value of the hedged brokered CDs and medium-term notes based on the expected call date of the instruments. The adoption of the fair value option also required the recognition, as part of the initial adoption adjustment to retained earnings, of all of the unamortized placement fees that were paid to broker counterparties upon the issuance of the elected brokered CDs and medium-term notes. The Corporation previously amortized those fees through earnings based on the expected call date of the instruments. The option of using fair value accounting also requires that the accrued interest be reported as part of the fair value of the financial instruments elected to be measured at fair value.

Income Recognition on Loans

Loans are stated at the principal outstanding balance, net of unearned interest, unamortized deferred origination fees and costs and unamortized premiums and discounts. Fees collected and costs incurred in the origination of new loans are deferred and amortized using the interest method or a method which approximates the interest method over the term of the loan as an adjustment to interest yield. Unearned interest on certain personal, auto loans and finance leases is recognized as income under a method which approximates the interest method. When a loan is paid off or sold, any unamortized net deferred fee (cost) is credited (charged) to income.

Loans on which the recognition of interest income has been discontinued are designated as non-accruing. When loans are placed on non-accruing status, any accrued but uncollected interest income is reversed and charged against interest income. Consumer, construction, commercial and mortgage loans are classified as non-accruing when interest and principal have not been received for a period of 90 days or more or when there are doubts about the potential to collect all of the principal based on collateral deficiencies or, in other situations, when collection of all of the principal or interest is not expected due to deterioration in the financial condition of the borrower. Interest income on non-accruing loans is recognized only to the extent it is received in cash. However, where there is doubt regarding the ultimate collectability of loan principal, all cash thereafter received is applied to reduce the carrying value of such loans (i.e., the cost recovery method). Loans are restored to accrual status only when future payments of interest and principal are reasonably assured.

Loan and lease losses are charged and recoveries are credited to the allowance for loan and lease losses. Closed-end personal consumer loans are charged-off when payments are 120 days in arrears. Collateralized auto and finance leases are reserved at 120 days delinquent and charged-off to their estimated net realizable value when collateral deficiency is deemed uncollectible (i.e. when foreclosure is probable). Open-end (revolving credit)

consumer loans are charged-off when payments are 180 days in arrears.

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A loan is considered impaired when, based upon current information and events, it is probable that the Corporation will be unable to collect all amounts due (including principal and interest) according to the contractual terms of the loan agreement. The Corporation measures impairment individually for those commercial and construction loans with a principal balance of \$1 million or more, including loans for which a charge-off has been recorded based upon the fair value of the underlying collateral, and also evaluates for impairment purposes certain residential mortgage loans with high delinquency and loan-to-value levels. Interest income on impaired loans is recognized based on the Corporation's policy for recognizing interest on accrual and non-accrual loans. Impaired loans also include loans that have been modified in troubled debt restructurings as a concession to borrowers experiencing financial difficulties. Troubled debt restructurings typically result from the Corporation's loss mitigation activities or programs sponsored by the Federal Government and could include rate reductions, principal forgiveness, forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of collateral. Troubled debt restructurings are generally reported as non-performing loans and restored to accrual status when there is a reasonable assurance of repayment and the borrower has made payments over a sustained period, generally six months. However, a loan that has been formally restructured as to be reasonably assured of repayment and of performance according to its modified terms is not placed in non-accruing status, provided the restructuring is supported by a current, well documented credit evaluation of the borrower's financial condition taking into consideration sustained historical payment performance for a reasonable time prior to the restructuring.

Recent Accounting Pronouncements

The FASB have issued the following accounting pronouncements and guidance relevant to the Corporation's operations:

In May 2008, the FASB issued authoritative guidance on financial guarantee insurance contracts requiring that an insurance enterprise recognize a claim liability prior to an event of default (insured event) when there is evidence that credit deterioration has occurred in an insured financial obligation. This guidance also clarifies how the accounting and reporting by insurance entities applies to financial guarantee insurance contracts, including the recognition and measurement to be used to account for premium revenue and claim liabilities. FASB authoritative guidance on the accounting for financial guarantee insurance contracts is effective for financial statements issued for fiscal years beginning after December 15, 2008, and all interim periods within those fiscal years, except for some disclosures about the insurance enterprise's risk-management activities which are effective since the first interim period after the issuance of this guidance. The adoption of this guidance did not have a significant impact on the Corporation's financial statements.

In June 2008, the FASB issued authoritative guidance for determining whether instruments granted in shared-based payment transactions are participating securities. This guidance applies to entities with outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends. Furthermore, awards with dividends that do not need to be returned to the entity if the employee forfeits the award are considered participating securities. Accordingly, under this guidance unvested share-based payment awards that are considered to be participating securities must be included in the computation of earnings per share (EPS) pursuant to the two-class method as required by FASB guidance on earnings per share. FASB guidance on determining whether instruments granted in share based payment transactions are participating securities is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those years. The adoption of this Statement did not have an impact on the Corporation's financial statements since, as of December 31, 2009, the outstanding unvested shares of restricted stock do not contain rights to nonforfeitable dividends.

In April 2009, the FASB issued authoritative guidance for the accounting of assets acquired and liabilities assumed in a business combination that arise from contingencies. This guidance amends the provisions related to the initial recognition and measurement, subsequent measurement and disclosure of assets and liabilities arising from contingencies in a business combination. The guidance carries forward the requirement that acquired contingencies in a business combination be recognized at fair value on the acquisition date if fair value can be reasonably estimated during the allocation period. Otherwise, entities would typically account for the acquired contingencies based on a reasonable estimate in accordance with FASB guidance on the accounting for contingencies. This guidance is effective for assets or liabilities arising from contingencies in business combinations for which the

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acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The adoption of this Statement did not have an impact on the Corporation's financial statements.

In April 2009, the FASB issued authoritative guidance for determining fair value when the volume and level of activity for the asset or liability have significantly decreased and identifying transactions that are not orderly. This guidance relates to determining fair values when there is no active market or where the price inputs being used represent distressed sales. It reaffirms the objective of fair value measurement, that is, to reflect how much an asset would be sold for in an orderly transaction (as opposed to a distressed or forced transaction) at the date of the financial statements under current market conditions. Specifically, it reaffirms the need to use judgment to ascertain if a formerly active market has become inactive and in determining fair values when markets have become inactive. This guidance is effective for interim and annual reporting periods ending after June 15, 2009 on a prospective basis. The adoption of this Statement did not impact the Corporation's fair value methodologies on its financial assets and liabilities.

In April 2009, the FASB amended the existing guidance on determining whether an impairment for investments in debt securities is OTTI and requires an entity to recognize the credit component of an OTTI of a debt security in earnings and the noncredit component in other comprehensive income (OCI) when the entity does not intend to sell the security and it is more likely than not that the entity will not be required to sell the security prior to recovery. This guidance also requires expanded disclosures and became effective for interim and annual reporting periods ending after June 15, 2009. In connection with this guidance, the Corporation recorded \$1.3 million for the year ended December 31, 2009 of OTTI charges through earnings that represents the credit loss of available-for-sale private label mortgage-backed securities. This guidance does not amend existing recognition and measurement guidance related to an OTTI of equity securities. The expanded disclosures related to this new guidance are included in *Note 4* of the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K.

In April 2009, the FASB amended the existing guidance on the disclosure about fair values of financial instruments, which requires entities to disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments, in both interim financial statements as well as annual financial statements. This guidance became effective for interim reporting periods ending after June 15, 2009. The adoption of the amended guidance expanded the Corporation's interim financial statement disclosures with regard to the fair value of financial instruments.

In May 2009, the FASB issued authoritative guidance on subsequent events, which establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. This guidance sets forth (i) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, (ii) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements and (iii) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. This guidance is effective for interim or annual financial periods ending after June 15, 2009. There are not any material subsequent event that would require further disclosure.

In June 2009, the FASB amended the existing guidance on the accounting for transfers of financial assets, which improves the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. This guidance is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Subsequently in December 2009, the FASB amended the existing guidance issued in June 2009. Among the most significant changes and additions to this guidance includes changes to the conditions for sales of a financial assets which objective is to determine whether a transferor and its consolidated affiliates included in the financial statements have surrendered control over transferred financial assets or third-party beneficial interests; and the addition of the meaning of the term participating interest which represents a proportionate (pro rata) ownership interest in an entire financial asset. The Corporation is evaluating the impact the adoption of the guidance will have on

its financial statements.

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In June 2009, the FASB amended the existing guidance on the consolidation of variable interest, which improves financial reporting by enterprises involved with variable interest entities and addresses (i) the effects on certain provisions of the amended guidance, as a result of the elimination of the qualifying special-purpose entity concept in the accounting for transfer of financial assets guidance and (ii) constituent concerns about the application of certain key provisions of the guidance, including those in which the accounting and disclosures do not always provide timely and useful information about an enterprise's involvement in a variable interest entity. This guidance is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Subsequently in December 2009, the FASB amended the existing guidance issued in June 2009. Among the most significant changes and additions to this guidance includes the replacement of the quantitative-based risks and rewards calculation for determining which reporting entity, if any, has a controlling financial interest in a variable interest entity with an approach focused on identifying which reporting entity has the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and the obligation to absorb losses of the entity or the right to receive benefits from the entity. The Corporation is evaluating the impact, if any, the adoption of this guidance will have on its financial statements.

In June 2009, the FASB issued authoritative guidance on the FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles. The FASB Accounting Standards Codification (Codification) is the single source of authoritative nongovernmental GAAP. Rules and interpretive releases of the SEC under the authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. The Codification project does not change GAAP in any way shape or form; it only reorganizes the existing pronouncements into one single source of U.S. GAAP. This guidance is effective for interim and annual periods ending after September 15, 2009. All existing accounting standards are superseded as described in this guidance. All other accounting literature not included in the Codification is nonauthoritative. Following this guidance, the FASB will not issue new guidance in the form of Statements, FASB Staff Positions, or Emerging Issues Task Force Abstracts. Instead, it will issue Accounting Standards Updates (ASUs). The FASB will not consider ASUs as authoritative in their own right. ASUs will serve only to update the Codification, provide background information about the guidance, and provide the bases for conclusions on the change(s) in the Codification.

In August 2009, the FASB updated the Codification in connection with the fair value measurement of liabilities to clarify that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value using one or more of the following techniques:

1. A valuation technique that uses:
 - a. The quoted price of the identical liability when traded as an asset
 - b. Quoted prices for similar liabilities or similar liabilities when traded as assets
2. Another valuation technique that is consistent with the principles of fair value measurement. Two examples would be an income approach, such as a present value technique, or a market approach, such as a technique that is based on the amount at the measurement date that the reporting entity would pay to transfer the identical liability or would receive to enter into the identical liability.

The update also clarifies that when estimating the fair value of a liability, a reporting entity is not required to include a separate input or adjustment to other inputs relating to the existence of a restriction that prevents the transfer of the liability. The update also clarifies that both a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustment to the quoted price of the asset are required are Level 1 fair value measurements. This update is effective for the first reporting period (including interim periods) beginning after issuance. The adoption of this guidance did not impact the Corporation's fair value methodologies on its financial liabilities.

In September 2009, the FASB updated the Codification to reflect SEC staff pronouncements on earnings-per-share calculations. According to the update, the SEC staff believes that when a public company redeems preferred shares, the difference between the fair value of the consideration transferred to the holders of the preferred stock and the carrying amount on the balance sheet after issuance costs of the preferred stock should be added to or subtracted from

net income before doing an earnings per share calculation. The SEC's staff also thinks it is not appropriate to aggregate preferred shares with different dividend yields when trying to determine whether the if-converted method is dilutive to the earnings per-share calculation. As of December 31, 2009, the Corporation has not been involved in a redemption or induced conversion of preferred stock.

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In January 2010, the FASB updated the Codification to provide guidance on accounting for distributions to shareholders with components of stock and cash. This guidance clarifies that the stock portion of a distribution to shareholders that allows them to elect to receive cash or stock with a potential limitation on the total amount of cash that all shareholders can elect to receive in the aggregate is considered a share issuance that is reflected in EPS prospectively and is not a stock dividend. The new guidance is effective for interim and annual periods ending on or after December 15, 2009, and would be applied on a retrospective basis. The adoption of this guidance did not impact the Corporation's financial statements.

In January 2010, the FASB updated the Codification to provide guidance to improve disclosure requirements related to fair value measurements and require reporting entities to make new disclosures about recurring or nonrecurring fair-value measurements including significant transfers into and out of Level 1 and Level 2 fair-value measurements and information on purchases, sales, issuances, and settlements on a gross basis in the reconciliation of Level 3 fair-value measurements. The FASB also clarified existing fair-value measurement disclosure guidance about the level of disaggregation, inputs, and valuation techniques. Entities will be required to separately disclose significant transfers into and out of Level 1 and Level 2 measurements in the fair-value hierarchy and the reasons for the transfers. Significance will be determined based on earnings and total assets or total liabilities or, when changes in fair value are recognized in other comprehensive income, based on total equity. A reporting entity must disclose and consistently follow its policy for determining when transfers between levels are recognized. Acceptable methods for determining when to recognize transfers include: (i) actual date of the event or change in circumstances causing the transfer; (ii) beginning of the reporting period; and (iii) end of the reporting period. Currently, entities are only required to disclose activity in Level 3 measurements in the fair-value hierarchy on a net basis. This guidance will require separate disclosures for purchases, sales, issuances, and settlements of assets. Entities will also have to disclose the reasons for the activity and apply the same guidance on significance and transfer policies required for transfers between Level 1 and 2 measurements. The guidance requires disclosure of fair-value measurements by class instead of major category. A class is generally a subset of assets and liabilities within a financial statement line item and is based on the specific nature and risks of the assets and liabilities and their classification in the fair-value hierarchy. When determining classes, reporting entities must also consider the level of disaggregated information required by other applicable GAAP. For fair-value measurements using significant observable inputs (Level 2) or significant unobservable inputs (Level 3), this guidance requires reporting entities to disclose the valuation technique and the inputs used in determining fair value for each class of assets and liabilities. If the valuation technique has changed in the reporting period (e.g., from a market approach to an income approach) or if an additional valuation technique is used, entities are required to disclose the change and the reason for making the change. Except for the detailed Level 3 roll forward disclosures, the guidance is effective for annual and interim reporting periods beginning after December 15, 2009 (first quarter of 2010 for public companies with calendar year-ends). The new disclosures about purchases, sales, issuances, and settlements in the roll forward activity for Level 3 fair-value measurements are effective for interim and annual reporting periods beginning after December 15, 2010 (first quarter of 2011 for public companies with calendar year-ends). Early adoption is permitted. In the initial adoption period, entities are not required to include disclosures for previous comparative periods; however, they are required for periods ending after initial adoption. The Corporation is evaluating the impact the adoption of this guidance will have on its financial statements.

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 year ended December 31, 2009 was \$519.0 million, compared to \$527.9 million and \$451.0 million for 2008 and 2007, respectively. On an adjusted 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 year ended December 31, 2009 was \$567.2 million, compared to \$579.1 million and \$475.4 million for 2008 and 2007, respectively.

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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 (for definition and reconciliation of this non-GAAP measure, refer to discussions below) and excluding: (1) the change in the fair value of derivative instruments, and (2) unrealized gains or losses on liabilities measured at fair value.

Part I

Period Ended December 31,	Average volume			Interest income ⁽¹⁾ / expense			Average rate ⁽¹⁾		
	2009	2008	2007	2009	2008	2007	2009	2008	2007
	(Dollars in thousands)								
Interest-earning assets:									
Money market & other									
Short-term investments	\$ 182,205	\$ 286,502	\$ 440,598	\$ 577	\$ 6,355	\$ 22,155	0.32%	2.22%	5.0%
Government obligations ⁽²⁾	1,345,591	1,402,738	2,687,013	54,323	93,539	159,572	4.04%	6.67%	5.9%
Mortgage-backed securities	4,254,044	3,923,423	2,296,855	238,992	244,150	117,383	5.62%	6.22%	5.1%
Corporate bonds	4,769	7,711	7,711	294	570	510	6.16%	7.39%	6.6%
FLB stock	76,982	65,081	46,291	3,082	3,710	2,861	4.00%	5.70%	6.1%
Municipality securities	2,071	3,762	8,133	126	47	3	6.08%	1.25%	0.0%
Real estate investments ⁽³⁾	5,865,662	5,689,217	5,486,601	297,394	348,371	302,484	5.07%	6.12%	5.5%
Interest-earning liabilities:									
Residential mortgage loans									
Construction loans	3,523,576	3,351,236	2,914,626	213,583	215,984	188,294	6.06%	6.44%	6.4%
Commercial and commercial	1,590,309	1,485,126	1,467,621	52,908	82,513	121,917	3.33%	5.56%	8.3%
Mortgage loans	6,343,635	5,473,716	4,797,440	263,935	314,931	362,714	4.16%	5.75%	7.5%
Finance leases	341,943	373,999	379,510	28,077	31,962	33,153	8.21%	8.55%	8.7%
Consumer loans	1,661,099	1,709,512	1,729,548	188,775	197,581	202,616	11.36%	11.56%	11.7%
Other loans ^{(4) (5)}	13,460,562	12,393,589	11,288,745	747,278	842,971	908,694	5.55%	6.80%	8.0%
Total interest-earning assets	\$ 19,326,224	\$ 18,082,806	\$ 16,775,346	\$ 1,044,672	\$ 1,191,342	\$ 1,211,178	5.41%	6.59%	7.2%
Interest-bearing liabilities:									
Interest-bearing checking									
Accounts	\$ 866,464	\$ 580,572	\$ 443,420	\$ 19,995	\$ 12,914	\$ 11,365	2.31%	2.22%	2.5%
Savings accounts	1,540,473	1,217,730	1,020,399	19,032	18,916	15,037	1.24%	1.55%	1.4%
Certificates of deposit	1,680,325	1,812,957	1,652,430	50,939	73,466	82,761	3.03%	4.05%	5.0%
Time-deposit CDs	7,300,696	7,671,094	7,639,470	227,896	318,199	415,287	3.12%	4.15%	5.4%
Interest-bearing deposits	11,387,958	11,282,353	10,755,719	317,862	423,495	524,450	2.79%	3.75%	4.8%
Loans payable	643,618	10,792		2,331	243		0.36%	2.25%	

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er borrowed funds	3,745,980	3,864,189	3,449,492	124,340	148,753	172,890	3.32%	3.85%	5.0
LB advances	1,322,136	1,120,782	723,596	32,954	39,739	38,464	2.49%	3.55%	5.3
al interest-bearing liabilities ⁽⁶⁾	\$ 17,099,692	\$ 16,278,116	\$ 14,928,807	\$ 477,487	\$ 612,230	\$ 735,804	2.79%	3.76%	4.9
interest income				\$ 567,185	\$ 579,112	\$ 475,374			
rest rate spread							2.62%	2.83%	2.2
interest margin							2.93%	3.20%	2.8

(1) On an adjusted tax-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 (40.95% for the Corporation's subsidiaries other than IBEs in 2009, 35.95% for the Corporation's IBEs in 2009 and 39% for all subsidiaries in 2008 and 2007) 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 instruments 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-accruing loans.
- (5) Interest income on loans includes \$11.2 million, \$10.2 million, and \$11.1 million for 2009, 2008 and 2007, 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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	2009 Compared to 2008			2008 Compared to 2007		
	Increase (decrease)			Increase (decrease)		
	Volume	Due to: Rate	Total	Volume	Due to: Rate	Total
	(In thousands)					
Interest income on interest-earning assets:						
Money market & other short-term investments	\$ (1,724)	\$ (4,054)	\$ (5,778)	\$ (6,082)	\$ (9,718)	\$ (15,800)
Government obligations	(3,672)	(35,544)	(39,216)	(80,954)	14,921	(66,033)
Mortgage-backed securities	19,474	(24,632)	(5,158)	97,011	29,756	126,767
Corporate bonds	(192)	(84)	(276)		60	60
FHLB stock	578	(1,206)	(628)	1,115	(266)	849
Equity securities	(62)	141	79	(29)	73	44
Total investments	14,402	(65,379)	(50,977)	11,061	34,826	45,887
Residential mortgage loans	10,716	(13,117)	(2,401)	28,173	(483)	27,690
Construction loans	4,681	(34,286)	(29,605)	1,214	(40,618)	(39,404)
C&I and commercial mortgage loans	43,028	(94,024)	(50,996)	45,020	(92,803)	(47,783)
Finance leases	(2,654)	(1,231)	(3,885)	(477)	(714)	(1,191)
Consumer loans	(5,466)	(3,340)	(8,806)	(2,332)	(2,703)	(5,035)
Total loans	50,305	(145,998)	(95,693)	71,598	(137,321)	(65,723)
Total interest income	64,707	(211,377)	(146,670)	82,659	(102,495)	(19,836)
Interest expense on interest-bearing liabilities:						
Brokered CDs	(14,707)	(75,596)	(90,303)	1,591	(98,679)	(97,088)
Other interest-bearing deposits	12,285	(27,615)	(15,330)	21,551	(25,418)	(3,867)
Loans payable	8,265	(6,177)	2,088	243		243
Other borrowed funds	(4,439)	(19,974)	(24,413)	18,327	(42,464)	(24,137)
FHLB advances	6,122	(12,907)	(6,785)	17,599	(16,324)	1,275
Total interest expense	7,526	(142,269)	(134,743)	59,311	(182,885)	(123,574)
Change in net interest income	\$ 57,181	\$ (69,108)	\$ (11,927)	\$ 23,348	\$ 80,390	\$ 103,738

A portion 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 sale of investments held by the Corporation's international banking entities are tax-exempt under the Puerto Rico tax law (refer to the Income Taxes discussion below for additional information regarding recent legislation that imposes a temporary 5% tax rate on IBEs' net income). 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 recent changes to enacted tax rates (40.95% for the Corporation's subsidiaries other than IBEs in 2009, 35.95% for the Corporation's IBEs in 2009 and 39% for all subsidiaries in 2008 and 2007) 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 "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 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 assets or interest-bearing liabilities, respectively, or on interest payments exchanged with interest rate swap counterparties.

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The following table reconciles the interest income on an adjusted tax-equivalent basis set forth in Part I above to interest income set forth in the Consolidated Statements of (Loss) Income:

<i>(In thousands)</i>	Year Ended December 31,		
	2009	2008	2007
Interest income on interest-earning assets on an adjusted tax-equivalent basis	\$ 1,044,672	\$ 1,191,342	\$ 1,211,178
Less: tax equivalent adjustments	(53,617)	(56,408)	(15,293)
Plus (less): net unrealized gain (loss) on derivatives	5,519	(8,037)	(6,638)
Total interest income	\$ 996,574	\$ 1,126,897	\$ 1,189,247

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:

<i>(In thousands)</i>	Year Ended December 31,		
	2009	2008	2007
Unrealized gain (loss) on derivatives (economic undesignated hedges):			
Interest rate caps	\$ 3,496	\$ (4,341)	\$ (3,985)
Interest rate swaps on loans	2,023	(3,696)	(2,653)
Net unrealized gain (loss) on derivatives (economic undesignated hedges)	\$ 5,519	\$ (8,037)	\$ (6,638)

The following table summarizes the components of interest expense for the years ended December 31, 2009, 2008 and 2007. As previously stated, the net interest margin analysis excludes the changes in the fair value of derivatives and unrealized gains or losses on liabilities measured at fair value:

<i>(In thousands)</i>	Year Ended December 31,		
	2009	2008	2007
Interest expense on interest-bearing liabilities	\$ 460,128	\$ 632,134	\$ 713,918
Net interest (realized) incurred on interest rate swaps	(5,499)	(35,569)	12,323
Amortization of placement fees on brokered CDs	22,858	15,665	9,056
Amortization of placement fees on medium-term notes			507
Interest expense excluding net unrealized loss (gain) on derivatives (economic undesignated hedges) and net unrealized (gain) loss on liabilities measured at fair value,	477,487	612,230	735,804
Net unrealized loss (gain) on derivatives (economic undesignated hedges) and liabilities measured at fair value	45	(13,214)	4,488
Accretion of basis adjustment	(2,061)		(2,061)
Total interest expense	\$ 477,532	\$ 599,016	\$ 738,231

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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:

<i>(In thousands)</i>	Year Ended December 31,		
	2009	2008	2007
Unrealized loss (gain) on derivatives (economic undesignated hedges):			
Interest rate swaps and other derivatives on brokered CDs	\$ 5,321	\$ (62,856)	\$ (66,826)
Interest rate swaps and other derivatives on medium-term notes	199	(392)	692
Net unrealized loss (gain) on derivatives (economic undesignated hedges)	5,520	(63,248)	(66,134)
Unrealized (gain) loss on liabilities measured at fair value:			
Unrealized (gain) loss on brokered CDs	(8,696)	54,199	71,116
Unrealized loss (gain) on medium-term notes	3,221	(4,165)	(494)
Net unrealized (gain) loss on liabilities measured at fair value:	(5,475)	50,034	70,622
Net unrealized loss (gain) on derivatives (economic undesignated hedges) and liabilities measured at fair value	\$ 45	\$ (13,214)	\$ 4,488

The following table summarizes the components of the accretion of basis adjustment which are included in interest expense in 2007:

	Year Ended December 31, 2007	
	(In thousands)	
Accretion of basis adjustments on fair value hedges:		
Interest rate swaps on brokered CDs	\$	
Interest rate swaps on medium-term notes		(2,061)
Accretion of basis adjustment on fair value hedges	\$	(2,061)

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, advances from the FHLB and FED, repurchase agreements and notes payable.

Net interest incurred or realized on interest rate swaps primarily represents net interest exchanged on swaps that economically hedge brokered CDs and medium-term notes.

The amortization of broker placement fees represents the amortization of fees paid to brokers upon issuance of related financial instruments (i.e., brokered CDs not elected for the fair value option). For 2007, the amortization of broker placement fees includes the derecognition of the unamortized balance of placement fees related to a \$150 million note redeemed prior to its contractual maturity during the second quarter as well as the amortization of placement fees for brokered CDs not elected for the fair value option.

Unrealized gains or losses on derivatives represents changes in the fair value of derivatives, primarily interest rate swaps, that economically hedge liabilities (i.e., brokered CDs and medium-term notes) or assets (i.e., loans and

investments).

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

For 2007, the basis adjustment represents the basis differential between the market value and the book value of a \$150 million medium-term note recognized at the inception of fair value hedge accounting on April 3, 2006, as well as changes in fair value recognized after the inception until the discontinuance of fair value hedge accounting on January 1, 2007, which was amortized or accreted based on the expected maturity of the liability as a yield adjustment. The unamortized balance of the basis adjustment was derecognized as part of the redemption of the \$150 million note resulting in an adjustment to earnings of \$1.9 million recognized as an accretion of basis adjustment, during the second quarter of 2007.

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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 December 31, 2009, most of the interest rate swaps outstanding are used for protection against rising interest rates. In the past, the volume of interest rate swaps was much higher, as they were used to convert the fixed-rate of a large portfolio of brokered CDs, mainly those with long-term maturities, to a variable rate and mitigate the interest rate risk related to variable rate loans. However, most of these interest rate swaps were called during 2009, due to lower interest rate levels. Refer to Note 32 of the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K 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.

2009 compared to 2008

Net interest income decreased 2% to \$519.0 million for 2009 from \$527.9 million for 2008 adversely impacted by a 27 basis points decrease, on an adjusted tax-equivalent basis, in the Corporation's net interest margin. The decrease in the yield of the Corporation's average interest-earning assets declined more than the cost of the average interest-bearing liabilities. The yield on interest-earning assets decreased 118 basis points to 5.41% for 2009 from 6.59% for 2008. The decrease was primarily the result of a lower yield on average loans which decreased 125 basis points to 5.55% for 2009 from 6.80% for 2008. The decrease in the yield on average loans was primarily due to the increase in non-accrual loans which resulted in the reversal of accrued interest. Also contributing to a lower yield on average loans was the decline in market interest rates that resulted in reductions in interest income from variable rate loans, primarily commercial and construction loans tied to short-term indexes, even though the Corporation is actively increasing spreads on loans renewals. The Corporation increased the use of interest rate floors in new commercial and construction loans agreements and renewals in 2009 to protect net interest margins going forward. The average 3-month LIBOR for 2009 was 0.69% compared to 2.93% for 2008 and the Prime Rate for 2009 was 3.25% compared to an average of 5.08% for 2008. Lower yields were also observed in the investment securities portfolio, driven by the approximately \$946 million of U.S. agency debentures called in 2009 and MBS prepayments, which were replaced with lower yielding investments financed with very low-cost sources of funding.

The cost of average-interest bearing liabilities decreased 97 basis to 2.79% for 2009 from 3.76% for 2008, primarily due to the decline short-term rates and changes in the mix of funding sources. The weighted-average cost of brokered CDs decreased 103 basis points to 3.12% for 2009 from 4.15% for 2008 primarily due to the replacement of maturing or callable brokered CDs that had interest rates above current market rates with shorter-term brokered CDs. Also, as a result of the general decline in market interest rates, lower interest rates were paid on existing customer money market and savings accounts coupled with lower interest rates paid on new deposits. In addition, the Corporation increased the use of short-term advances from the FHLB and the FED. The Corporation increased its short-term borrowings as a measure of interest rate risk management to match the shortening in the average life of the investment portfolio and shifted the funding emphasis to retail deposit to reduce reliance on brokered CDs.

Partially offsetting the compression in net interest margin, was an increase of \$1.2 billion in average interest-earning assets. The higher volume of average interest-earning assets was driven by the growth of the C&I loan portfolio in Puerto Rico, primarily due to credit facilities extended to the Puerto Rico Government and its political subdivisions. Also, funds obtained through short-term borrowings were invested, in part, in the purchase of investment securities to mitigate the decline in the average yield on securities that resulted from the acceleration of MBS prepayments and calls of U.S. agency debentures.

On an adjusted tax-equivalent basis, net interest income decreased by \$11.9 million, or 2%, for 2009 compared to 2008. The decrease was principally due to lower yields on earning-assets as described above and a decrease of \$2.8 million in the tax-equivalent adjustment. 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 the interest rate spread on tax-exempt assets, mainly due to lower yields on U.S. agency

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debentures an MBS held by the Corporation's IBE subsidiary, as the Corporation replaced securities called and sold as well as prepayments of MBS with shorter-term securities, and due to the decrease in income tax savings on securities held by FirstBank Overseas Corporation resulting from the temporary 5% tax imposed in 2009 to all IBEs (see Income Taxes discussion below).

2008 compared to 2007

Net interest income increased 17% to \$527.9 million for 2008 from \$451.0 million for 2007. Approximately \$14.2 million of the total net interest income increase was related to fluctuations in the fair value of derivative instruments and financial liabilities measured at fair value. The Corporation's net interest spread and margin for 2008, on an adjusted tax equivalent basis, were 2.83% and 3.20%, respectively, up 54 and 37 basis points from 2007. The increase was mainly associated with a decrease in the average cost of funds resulting from lower short-term interest rates and, to a lesser extent, a higher volume of interest earning assets. During 2008, the target for the Federal Funds rate was lowered from 4.25% to a range of 0% to 0.25% through seven separate actions in an attempt to stimulate the U.S. economy, officially in recession since December 2007. The decrease in funding costs more than offset lower loan yields resulting from the repricing of variable-rate construction and commercial loans tied to short-term indexes and from a higher volume of non-accrual loans.

Average earning assets for 2008 increased by \$1.3 billion, as compared to 2007, driven by commercial and residential real estate loan originations, and, to a lesser extent, purchases of loans during 2008 that contributed to a wider spread. In addition, the Corporation purchased approximately \$3.2 billion in U.S. government agency fixed-rate MBS having an average yield of 5.44% during 2008, which is higher than the cost of the borrowing required to finance the purchase of such assets, thus contributing to a higher net interest income as compared to 2007. The increase in the loan and MBS portfolio was partially offset by the early redemption, through call exercises, of approximately \$1.2 billion of U.S. Agency debentures with an average yield of 5.87% due to the drop in rates in the long end of the yield curve.

On the funding side, the average cost of the Corporation's interest-bearing liabilities decreased by 117 basis points mainly due to lower short-term rates and the mix of borrowings. The benefit from the decline in short-term rates in 2008 was partially offset by the Corporation's strategy, in managing its asset/liability position in order to limit the effects of changes in interest rates on net interest income, of reducing its exposure to high levels of market volatility by, among other things, extending the duration of its borrowings and replacing swapped-to-floating brokered CDs that matured or were called (due to lower short-term rates) with brokered CDs not hedged with interest rate swaps. Also, the Corporation has reduced its interest rate risk through other funding sources and by, among other things, entering into long-term and structured repurchase agreements that replaced short-term borrowings. The volume of swapped-to-floating brokered CDs decreased by approximately \$3.0 billion to \$1.1 billion as of December 31, 2008 from \$4.1 billion as of December 31, 2007.

On the asset side, the average yield of the Corporation's interest-earning assets decreased by 63 basis points driven by lower yields on the variable-rate commercial and construction loan portfolio. The weighted-average yield on loans decreased by 125 basis points during 2008. In the latter part of 2008, the Corporation took initial steps to obtain higher pricing on its variable-rate commercial loan portfolio; however, this effort was severely impacted by significant declines in short-term rates during the last quarter of 2008 (the Prime Rate dropped to 3.25% from 7.25% at December 31, 2007 and 3-month LIBOR closed at 1.43% on December 31, 2008 from 4.70% on December 31, 2007) and, to a lesser extent, by the increase in the volume of non-performing loans. Lower loans yields were partially offset by higher yields on tax-exempt securities such as U.S. agency MBS held by the Corporation's international banking entity subsidiary.

On an adjusted tax equivalent basis, net interest income increased by \$103.7 million, or 22%, for 2008 compared to 2007. The increase was principally due to the lower short-term rates discussed above but also was positively impacted by a \$41.1 million increase in the tax-equivalent adjustment. The increase in the tax-equivalent adjustment was mainly related to increases in the interest rate spread on tax-exempt assets due to lower short-term rates and a higher volume of tax-exempt MBS held by the Corporation's international banking entity subsidiary, FirstBank Overseas Corporation.

Table of Contents**Provision 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.

During 2009, the Corporation recorded a provision for loan and lease losses of \$579.9 million, compared to \$190.9 million in 2008 and \$120.6 million in 2007.

2009 compared to 2008

The increase, as compared to 2008, was mainly related to:

Increases in specific reserves for construction and commercial impaired loans.

Increases in non-performing and net charge-offs levels.

The migration of loans to higher risk categories, thus requiring higher general reserves.

The overall growth of the loan portfolio.

Even though the deterioration in credit quality was observed in all of the Corporation's portfolios, it was more significant in the construction and C&I loan portfolios, which were affected by the stagnant housing market and further deterioration in the economies of the markets served. The provision for loan losses for the construction loan portfolio increased by \$211.1 million and the provision for the C&I loan portfolio increased by \$110.6 million compared to 2008. This increase accounts for approximately 83% of the increase in the provision. As mentioned above, the increase was mainly driven by the migration of loans to higher risk categories, increases in specific reserves for impaired loans, and increases to loss factors used to determine the general reserve to account for negative trends in non-performing loans, charge-offs affected by declines in collateral values and economic indicators. The provision for residential mortgages also increased significantly for 2009, as compared to 2008, an increase of \$32 million, as a result of updating general reserve factors and a higher portfolio of delinquent loans evaluated for impairment purposes that was adversely impacted by decreases in collateral values.

In terms of geography, the Corporation recorded a \$366.0 million provision in 2009 for its loan portfolio in Puerto Rico compared to \$125.0 million in 2008, an increase of \$241.0 million mainly related to the C&I and construction loans portfolio. The provision for C&I loans in Puerto Rico increased by \$116.5 million and the provision for the construction loan portfolio in Puerto Rico increased by \$101.3 million. Rising unemployment and the depressed economy negatively impacted borrowers and was reflected in a persistent decline in the volume of new housing sales and underperformance of important sectors of the economy.

With respect to the United States loan portfolio, the Corporation recorded a \$188.7 million provision in 2009 compared to a \$53.4 million provision in 2008, an increase of \$135.3 million mainly related to the construction loan portfolio. The provision for construction loans in the United States increased by \$95.0 million compared to 2008, primarily due to charges against specific reserves for impaired construction projects, mainly collateral dependent loans that were charged-off to their collateral value in 2009 (refer to the Risk Management Credit Risk Management Allowance for Loan and Lease Losses and Non-performing Assets discussion below for additional information about charge-offs recorded in 2009). Impaired loans in the United States increased from \$210.1 million at December 31, 2008 to \$461.1 million by the end of 2009. As of December

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31, 2009, approximately 89%, or \$265.1 million of the total exposure to construction loans in Florida was individually measured for impairment.

The provision recorded for the loan portfolio in the Virgin Islands amounted to \$25.2 million in 2009, an increase of \$12.7 million compared to 2008 mainly related to the construction loan portfolio.

Refer to the discussions under Risk Management Credit Risk Management Allowance for Loan and Lease Losses and Non-performing Assets below for analysis of the allowance for loan and lease losses, non-performing assets, impaired loans and related information.

2008 compared to 2007

The increase, as compared to 2007, was mainly attributable to the significant increase in delinquency levels and increases in specific reserves for impaired commercial and construction loans adversely impacted by deteriorating economic conditions in the United States and Puerto Rico. Also, increases to reserve factors for potential losses inherent in the loan portfolio, higher reserves for the residential mortgage loan portfolio in the U.S. mainland and Puerto Rico and the overall growth of the Corporation's loan portfolio contributed to higher charges in 2008.

During 2008, the Corporation experienced continued stress in the credit quality of and worsening trends on its construction loan portfolio, in particular, condo-conversion loans affected by the continuing deterioration in the health of the economy, an oversupply of new homes and declining housing prices in the United States. The total exposure of the Corporation to condo-conversion loans in the United States was approximately \$197.4 million or less than 2% of the total loan portfolio. A total of approximately \$154.4 million of this condo conversion portfolio was considered impaired with a specific reserve of \$36.0 million allocated to these impaired loans during 2008. Absorption rates in condo-conversion loans in the United States were low and properties collateralizing some loans originally disbursed as condo-conversion were formally reverted to rental properties with a future plan for the sale of converted units upon an improvement in the United States real estate market. Higher reserves were also necessary for the residential mortgage loan portfolio in the U.S. mainland in light of increased delinquency levels and the decrease in housing prices.

In Puerto Rico, the Corporation's impaired commercial and construction loan portfolio amounted to approximately \$164 million and \$106 million, respectively, with specific reserves of \$21 million and \$19 million, respectively, allocated to these loans during 2008. The Corporation also increased its reserves for the residential mortgage and construction loan portfolio from the 2007 levels to account for the increased credit risk tied to recessionary conditions in Puerto Rico's economy.

Refer to the discussions under Financial Condition and Operating Analysis Lending Activities and under Risk Management Credit Risk Management below for additional information concerning the Corporation's loan portfolio exposure to the geographic areas where the Corporation does business.

Table of Contents**Non-interest Income**

The following table presents the composition of non-interest income:

	2009	2008 (In thousands)	2007
Other service charges on loans	\$ 6,830	\$ 6,309	\$ 6,893
Service charges on deposit accounts	13,307	12,895	12,769
Mortgage banking activities	8,605	3,273	2,819
Rental income	1,346	2,246	2,538
Insurance income	8,668	10,157	10,877
Other operating income	18,362	18,570	13,595
Non-interest income before net gain (loss) on investments, insurance reimbursement and other agreements related to a contingency settlement, net gain on partial extinguishment and recharacterization of secured commercial loans to local financial institutions and gain on sale of credit card portfolio	57,118	53,450	49,491
Gain on VISA shares and related proceeds	3,784	9,474	
Net gain on sale of investments	83,020	17,706	3,184
OTTI on equity securities and corporate bonds	(388)	(5,987)	(5,910)
OTTI on debt securities	(1,270)		
Net gain (loss) on investments	85,146	21,193	(2,726)
Insurance reimbursement and other agreements related to a contingency settlement			15,075
Gain on partial extinguishment and recharacterization of secured commercial loans to local financial institutions			2,497
Gain on sale of credit card portfolio			2,819
Total	\$ 142,264	\$ 74,643	\$ 67,156

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.

Rental income represents income generated by the Corporation's subsidiary, First Leasing, on the rental of various types of motor vehicles. As part of its strategies to focus on its core business, the Corporation divested its short-term rental business during the fourth quarter of 2009.

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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 other-than-temporary impairment charges (OTTI) on the Corporation's investment portfolio.

2009 compared to 2008

Non-interest income increased \$67.6 million to \$142.3 million for 2009, primarily reflecting:

- § A \$59.6 million increase in realized gains on the sale of investment securities, primarily reflecting a \$79.9 million gain on the sale of MBS (mainly U.S. agency fixed-rate MBS), compared to realized gains on the sale of MBS of \$17.7 million in 2008. In an effort to manage interest rate risk, and take advantage of favorable market valuations, approximately \$1.8 billion of U.S. agency MBS (mainly 30 Year fixed-rate U.S. agency MBS) were sold in 2009, compared to approximately \$526 million of U.S. agency MBS sold in 2008.
- § A \$5.3 million increase in gains from mortgage banking activities, due to the increased volume of loan sales and securitizations. Servicing assets recorded at the time of sale amounted to \$6.1 million for 2009 compared to \$1.6 million for 2008. The increase is mainly related to \$4.6 million of capitalized servicing assets in connection with the securitization of approximately \$305 million FHA/VA mortgage loans into GNMA MBS. For the first time in several years, the Corporation has been engaged in the securitization of mortgage loans in 2009.
- § A \$5.6 million decrease in OTTI charges related to equity securities and corporate bonds, partially offset by OTTI charges through earnings of \$1.3 million in 2009 related to the credit loss portion of available-for-sale private label MBS.

Also contributing to the increase in non-interest income was higher fee income, mainly fees on loans and service charges on deposit accounts offset by lower income from insurance activities and a reduction in income from vehicle rental activities. During the first three quarters of 2009, income from rental activities decreased by \$0.5 million due to a lower volume of business. A further reduction of \$0.4 million was observed in the fourth quarter of 2009, as compared to the comparable period in 2008, mainly related to the disposition of the Corporation's vehicle rental business early in the quarter, which was partially offset by a \$0.2 million gain recorded for the disposition of the business.

2008 compared to 2007

Non-interest income increased 11% to \$74.6 million for 2008 from \$67.2 million for 2007. The increase was related to a realized gain of \$17.7 million on the sale of approximately \$526 million of U.S. sponsored agency fixed-rate MBS and to the gain of \$9.3 million on the sale of part of the Corporation's investment in VISA in connection with VISA's IPO. The announcement of the FED that it will invest up to \$600 billion in obligations from U.S. government-sponsored agencies, including \$500 billion in MBS backed by FNMA, FHLMC and GNMA, caused a surge in prices and sent mortgage rates down and offered a market opportunity to realize a gain. Higher point of sale (POS) and ATM interchange fee income and an increase in fee income from cash management services provided to corporate customers accounted for approximately \$3.9 million of the increase in non-interest income. OTTI charges amounted to \$6.0 million in 2008, compared to \$5.9 million in 2007. Different from 2007 when impairment charges related exclusively to equity securities, most of the impairment charges in 2008 (approximately \$4.2 million) was related to auto industry corporate bonds held by FirstBank Florida. The Corporation's remaining exposure to auto industry corporate bonds as of December 31, 2008 amounted to \$1.5 million, while its exposure to equity securities was approximately \$2.2 million. These auto industry corporate bonds were sold in 2009 and a gain of \$0.9 million was recorded at the time of sale, while

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the exposure to equity securities was reduced to \$1.8 million as of December 31, 2009 after OTTI charges of \$0.4 million recorded in 2009

The increase in non-interest income attributable to activities mentioned above was partially offset, when comparing 2008 to 2007, by isolated events such as the \$15.1 million income recognition in 2007 for reimbursement of expenses related to the class action lawsuit settled in 2007, and a gain of \$2.8 million on the sale of a credit card portfolio and of \$2.5 million on the partial extinguishment and recharacterization of a secured commercial loan to a local financial institution that were recognized in 2007.

Non-Interest Expense

The following table presents the components of non-interest expenses:

	2009	2008 (In thousands)	2007
Employees compensation and benefits	\$ 132,734	\$ 141,853	\$ 140,363
Occupancy and equipment	62,335	61,818	58,894
Deposit insurance premium	40,582	10,111	6,687
Other taxes, insurance and supervisory fees	20,870	22,868	21,293
Professional fees recurring	12,980	12,572	13,480
Professional fees non-recurring	2,237	3,237	7,271
Servicing and processing fees	10,174	9,918	6,574
Business promotion	14,158	17,565	18,029
Communications	8,283	8,856	8,562
Net loss on REO operations	21,863	21,373	2,400
Other	25,885	23,200	24,290
Total	\$ 352,101	\$ 333,371	\$ 307,843

2009 compared to 2008

Non-interest expenses increased \$18.7 million to \$352.1 million for 2009 primarily reflecting:

- § An increase of \$30.5 million in the FDIC deposit insurance premium, including \$8.9 million for the special assessment levied by the FDIC in 2009 and increases in regular assessment rates. The FDIC increased its insurance premium rates to banks in 2009 due to losses to the FDIC insurance fund as a result of bank failures during 2008 and 2009, coupled with additional losses that the FDIC projected for the future due to anticipated additional bank failures.
- § A \$4.0 million impairment of the core deposit intangible of FirstBank Florida, recorded in 2009 as part of other non-interest expenses. The core deposit intangible represents the value of the premium paid to acquire core deposits of an institution. Core deposit intangible impairment occurs when the present value of expected future earnings attributed to maintaining the core deposit base diminishes. Factors which contributed to the impairment include deposit run-off and a shift of customers to time certificates.
- § A \$1.8 million increase in the reserve for probable losses on outstanding unfunded loan commitments recorded as part of other non-interest expenses. The reserve for unfunded loan commitments is an estimate of the losses inherent in off-balance sheet loan commitments at the balance sheet date, and it was mainly related to outstanding construction loans commitments. 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.

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The aforementioned increases were partially offset by decreases in certain controllable expenses such as:

§ A \$9.1 million decrease in employees' compensation and benefit expenses, mainly due to a lower headcount and reductions in bonuses, incentive compensation and overtime costs. The number of full time equivalent employees decreased by 163, or 6%, during 2009.

§ A \$3.4 million decrease in business promotion expenses due to a lower level of marketing activities.

§ A \$1.1 million decrease in taxes, other than income taxes, mainly driven by a decrease in municipal taxes which are assessed based on taxable gross revenues.

The Corporation continued to reduce costs through corporate-wide efforts to focus on its core business, including cost-cutting initiatives. The efficiency ratio for 2009 was 53.24% compared to 55.33% for 2008.

2008 compared to 2007

Non-interest expenses increased 8% to \$333.4 million for 2008 from \$307.8 million for 2007. The increase was principally attributable to a higher net loss on REO operations and increases in the deposit insurance premium expense and occupancy and equipment expenses, partially offset by lower professional fees.

The net loss on REO operations increased by approximately \$19.0 million for 2008, as compared to the previous year, mainly due to a higher inventory of repossessed properties and declining real estate prices, mainly in the U.S. mainland, that have caused write-downs of the value of repossessed properties. A significant portion of the losses was related to foreclosed properties in Florida, including a \$5.3 million write-down to the value of a single foreclosed project in the United States as of December 31, 2008. Higher losses were also observed in Puerto Rico due to a higher inventory and recent trends in sales.

The deposit insurance premium expense increased by \$3.4 million as the Corporation used available one-time credits to offset the premium increase in 2007 resulting from a new assessment system adopted by the FDIC and also attributable to the increase in the deposit base.

Occupancy and equipment expenses increased by \$2.9 million primarily to support the growth of the Corporation's operations as well as increases in utility costs.

Employees' compensation and benefit expenses increased by \$1.5 million for 2008, as compared to the previous year, primarily due to higher average compensation and related fringe benefits, partially offset by a decrease of \$2.8 million in stock-based compensation expenses and the impact in 2007 of the accrual of approximately \$3.3 million for a voluntary separation program established by the Corporation as part of its cost saving strategies. The Corporation has been able to continue the growth of its operations without incurring substantial additional operating expenses. The Corporation's total headcount decreased as compared to December 31, 2007 as a result of the voluntary separation program completed earlier in 2008 and reductions by attrition. These decreases have been partially offset by increases due to the acquisition of the Virgin Islands Community Bank (VICB) in the first quarter of 2008 and to reinforcement of audit and credit risk management personnel.

Professional fees decreased by \$4.9 million for the 2008 year, as compared to 2007, primarily attributable to lower legal, accounting and consulting fees due to, among other things, the settlement of legal and regulatory matters.

Table of Contents**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 creditable against the Corporation's Puerto Rico tax liability, subject to certain conditions and limitations.

Under the Puerto Rico Internal Revenue Code of 1994, as amended (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 capital gain statutory tax rate from 15% to 15.75%. This temporary measure is 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 IBEs of the Corporation and the Bank 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 IBEs are subject to a 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. The IBEs 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.

For additional information relating to income taxes, see Note 27 to the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K, including the reconciliation of the statutory to the effective income tax rate for 2009, 2008 and 2007.

2009 compared to 2008

For 2009, the Corporation recognized an income tax expense of \$4.5 million, compared to an income tax benefit of \$31.7 million for 2008. The fluctuation in income tax expense for 2009 mainly resulted from non-cash charges of approximately \$184.4 million to increase the valuation allowance for the Corporation's deferred tax asset. As of December 31, 2009, the deferred tax asset, net of a valuation allowance of \$191.7 million, amounted to \$109.2 million compared to \$128.0 million as of December 31, 2008.

Accounting for income taxes requires that companies assess whether a valuation allowance should be recorded against their deferred tax assets 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 reversing 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 recognized tax benefits only when deemed probable.

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In assessing the weight of positive and negative evidence, a significant negative factor that resulted in the increase of the valuation allowance was that the Corporation's banking subsidiary FirstBank Puerto Rico was in a three-year historical cumulative loss as of the end of the year 2009, mainly as a result of charges to the provision for loan and lease losses, especially in the construction portfolio both in Puerto Rico and the United States, resulting from the economic downturn. As of December 31, 2009, management concluded that \$109.2 million of the deferred tax assets will be realized. In assessing the likelihood of realizing the deferred tax assets, management has considered all four sources of taxable income mentioned above and even though sufficient profits are expected in the next seven years to realized the deferred tax asset, given current uncertain economic conditions, the Company has only relied on tax-planning strategies as the main source of taxable income to realize the deferred tax asset amount. Among the most significant tax-planning strategies identified are: (i) sale of appreciated assets, (ii) consolidation of profitable and unprofitable companies (in Puerto Rico each Company files a separate tax return; no consolidated tax returns are permitted), and (iii) deferral of deductions without affecting its utilization. Management will continue monitoring the likelihood of realizing the deferred tax assets in future periods. If future events differ from management's December 31, 2009 assessment, an additional valuation allowance may need to be established which may have a material adverse effect on the Corporation's results of operations. Similarly, to the extent the realization of a portion, or all, of the tax asset becomes more 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 increase in the valuation allowance does not have any impact on the Corporation's liquidity, nor does such an allowance preclude the Corporation from using tax losses, tax credits or other deferred tax assets in the future.

Partially offsetting the impact of the increase in the valuation allowance, was the reversal of approximately \$19 million of Unrecognized Tax Benefits (UTBs) as further discussed below. The income tax provision in 2009 was also impacted by adjustments to deferred tax amounts as a result of the aforementioned changes to the PR Code enacted tax rates. The effect of a higher temporary statutory tax rate over the normal statutory tax rate resulted in an additional income tax benefit of \$10.4 million for 2009 that was partially offset by an income tax provision of \$6.6 million related to the special 5% tax on the operations of FirstBank Overseas Corporation. Deferred tax amounts have been adjusted for the effect of the change in the income tax rate considering the enacted tax rate expected to apply to taxable income in the period in which the deferred tax asset or liability is expected to be settled or realized.

During the second quarter of 2009, the Corporation reversed UTBs by \$10.8 million and related accrued interest of \$5.3 million due to the lapse of the statute of limitations for the 2004 taxable year. Also, in July 2009, the Corporation entered into an agreement with the Puerto Rico Department of the Treasury to conclude an income tax audit and to eliminate all possible income and withholding tax deficiencies related to taxable years 2005, 2006, 2007 and 2008. As a result of such agreement, the Corporation reversed during the third quarter of 2009 the remaining UTBs and related interest by approximately \$2.9 million, net of the payment made to the Puerto Rico Department of the Treasury in connection with the conclusion of the tax audit. There were no UTBs outstanding as of December 31, 2009. Refer to Note 27 to the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K for additional information.

2008 compared to 2007

For 2008, the Corporation recognized an income tax benefit of \$31.7 million compared to an income tax expense of \$21.6 million for 2007. The fluctuation was mainly related to lower taxable income. A significant portion of revenues was derived from tax-exempt assets and operations conducted through the IBE, FirstBank Overseas Corporation. Also, the positive fluctuation in financial results was impacted by two transactions: (i) a reversal of \$10.6 million of UTBs during the second quarter of 2008 for positions taken on income tax returns, as explained below, and (ii) the recognition of an income tax benefit of \$5.4 million in connection with an agreement entered into with the Puerto Rico Department of Treasury during the first quarter of 2008 that established a multi-year allocation schedule for deductibility of the \$74.25 million payment made by the Corporation during 2007 to settle a securities class action suit. Also, higher deferred tax benefits were recorded in connection with a higher provision for loan and lease losses.

During the second quarter of 2008, the Corporation reversed UTBs of approximately \$7.1 million and accrued interest of \$3.5 million as a result of a lapse of the applicable statute of limitations for the 2003 taxable year.

Table of Contents**OPERATING SEGMENTS**

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 December 31, 2009, 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. For information regarding First BanCorp's reportable segments, please refer to Note 33 Segment Information to the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this Form 10-K.

Starting in the fourth quarter of 2009, the Corporation has realigned its reporting segments to better reflect how it views and manages its business. Two additional operating segments were created to evaluate the operations conducted by the Corporation outside of Puerto Rico. Operations conducted in the United States and in the Virgin Islands are now individually evaluated as separate operating segments. This realignment in the segment reporting essentially reflects the effect of restructuring initiatives, including the merger of FirstBank Florida operations with and into FirstBank, and will allow the Corporation to better present the results from its growth focus. Prior to the third quarter of 2009, the operating segments were driven primarily by the Corporation's legal entities. FirstBank operations conducted in the Virgin Islands and through its loan production office in Miami, Florida were reflected in the Corporation's then four reportable segments (Commercial and Corporate Banking; Mortgage Banking; Consumer (Retail) Banking; Treasury and Investments) while the operations conducted by FirstBank Florida were reported as part of a category named "Other". In the third quarter of 2009, as a result of the aforementioned merger, the operations of FirstBank Florida were reported as part of the four reportable segments. The change in the fourth quarter reflected a further realignment of the organizational structure as a result of management changes. Prior period amounts have been reclassified to conform to current period presentation. These changes did not have an impact on the previously reported consolidated results of the Corporation.

The accounting policies of the segments are the same as those described in Note 1 Nature of Business and Summary of Significant Accounting Policies to the Corporation's financial statements for the year ended December 31, 2009 included in Item 8 of this 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 Treasury and Investment segment lends funds to the Consumer (Retail) Banking, Mortgage Banking and Commercial and Corporate Banking segments to finance their lending activities and borrows funds from those segments. The Consumer (Retail) Banking segment also lends funds to other segments. The interest rates charged or credited by Treasury and Investment and the Consumer (Retail) Banking 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.

Consumer(Retail)Banking

The Consumer (Retail) Banking segment mainly consists of the Corporation's consumer lending and deposit-taking activities conducted mainly through its branch network and loan centers in Puerto Rico. Loans to consumers include auto, boat, lines of credit, personal loans and finance leases. Deposit products include interest bearing and non-interest bearing checking and savings accounts, Individual Retirement Accounts (IRA) and retail certificates of deposit. Retail

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deposits gathered through each branch of FirstBank's retail network serve as one of the funding sources for the lending and investment activities.

Consumer lending has been mainly driven by auto loan originations. The Corporation follows a strategy of seeking to provide outstanding service to selected auto dealers that provide the channel for the bulk of the Corporation's auto loan originations. This strategy is directly linked to our commercial lending activities as the Corporation maintains strong and stable auto floor plan relationships, which are the foundation of a successful auto loan generation operation. The Corporation's commercial relations with floor plan dealers are strong and directly benefit the Corporation's consumer lending operation and are managed as part of the consumer banking activities.

Personal loans and, to a lesser extent, marine financing and a small revolving credit portfolio also contribute to interest income generated on consumer lending. Credit card accounts are issued under the Bank's name through an alliance with FIA Card Services (Bank of America), which bears the credit risk. Management plans to continue to be active in the consumer loans market, applying the Corporation's strict underwriting standards. Other activities included in this segment are finance leases and insurance activities in Puerto Rico.

The highlights of the Consumer (Retail) Banking segment financial results for the year ended December 31, 2009 include the following:

Segment income before taxes for the year ended December 31, 2009 was \$20.9 million compared to \$21.8 million and \$37.8 million for the years ended December 31, 2008 and 2007, respectively.

Net interest income for the year ended December 31, 2009 was \$149.6 million compared to \$166.0 million and \$174.3 million for the years ended December 31, 2008 and 2007, respectively. The decrease in net interest income reflects a diminished consumer loan portfolio due to principal repayments and charge-offs relating to the auto and personal loans portfolio (including finance leases). This portfolio is mainly composed of fixed-rate loans financed with shorter-term borrowings thus positively affected in a declining interest rate scenario; however, this was more than offset by a decrease in the amount credited to this segment for its deposit-taking activities due to the decline in interest rates and the lower volume of loans, resulting in a decrease in net interest income in 2009 as compared to 2008 and in 2008 as compared to 2007.

The provision for loan and lease losses for 2009 decreased by \$18.0 million compared to the same period in 2008 and increased by \$6.7 million when comparing 2008 with the same period in 2007. The decrease in the provision was mainly related to the lower amount of the consumer loan portfolio, a relative stability in delinquency and non-performing levels, and a decrease in net charge-offs attributable in part to the changes in underwriting standards implemented since late 2005 and the originations using these new underwriting standards of new consumer loans to replace maturing consumer loans that had an average life of approximately four years. The increase in 2008, compared to 2007, was due to adjustments to loss factors based on economic indicators.

Non-interest income for the year ended December 31, 2009 was \$32.0 million compared to \$35.6 million and \$32.5 million for the years ended December 31, 2008 and 2007, respectively. The decrease for 2009, as compared to 2008, was mainly related to lower insurance income and a reduction in income from vehicle rental activities partially offset by higher service charges on deposit accounts and higher ATM interchange fee income. As part of the Corporation's strategies to focus on its core business, the Corporation divested its short-term rental business during the fourth quarter of 2009. The increase for 2008, as compared to 2007, was mainly related to higher point of sale (POS) and ATM interchange fee income caused by a change in the calculation of interchange fees charged between financial institutions in Puerto Rico from a fixed fee calculation to a percentage of the sale calculation since the second half of 2007.

Direct non-interest expenses for the year ended December 31, 2009 were \$98.3 million compared to \$99.2 million and \$95.2 million for the years ended December 31, 2008 and 2007, respectively. The decrease in direct non-interest expenses for 2009, as compared to 2008, was primarily due to reductions in

marketing and occupancy expenses, mainly electricity costs, partially offset by the increase in the FDIC insurance premium associated with increases in the regular assessment rates and the special fee levied in 2009. The increase in direct non-interest expenses for 2008, compared to 2007, was mainly due to increases in compensation, marketing collection efforts and the FDIC insurance premium.

Table of Contents*Commercial and Corporate Banking*

The Commercial and Corporate Banking segment consists of the Corporation's lending and other services for the public sector and specialized industries such as healthcare, tourism, financial institutions, food and beverage, shopping centers and middle-market clients. The Commercial and Corporate Banking segment offers commercial loans, including commercial real estate and construction loans, and other products such as cash management and business management services. A substantial portion of this portfolio is secured by the underlying value of the real estate collateral, and collateral and the personal guarantees of the borrowers are taken in abundance of caution. Although commercial loans involve greater credit risk than a typical residential mortgage loan because they are larger in size and more risk is concentrated in a single borrower, the Corporation has and maintains a credit risk management infrastructure designed to mitigate potential losses associated with commercial lending, including strong underwriting and loan review functions, sales of loan participations and continuous monitoring of concentrations within portfolios.

For this segment, the Corporation follows a strategy aimed to cater to customer needs in the commercial loans middle market segment by seeking to build strong relationships and offering financial solutions that meet customers unique needs. Starting in 2005, the Corporation expanded its distribution network and participation in the commercial loans middle market segment by focusing on customers with financing needs of up to \$5 million. The Corporation established 5 regional offices that provide coverage throughout Puerto Rico. The offices are staffed with sales, marketing and credit officers able to provide a high level of personalized service and prompt decision-making.

The highlights of the Commercial and Corporate Banking segment financial results for the year ended December 31, 2009 include the following:

Segment loss before taxes for the year ended December 31, 2009 was \$129.8 million compared to income of \$56.9 million and \$78.6 million for the years ended December 31, 2008 and 2007, respectively.

Net interest income for the year ended December 31, 2009 was \$180.3 million compared to \$112.3 million and \$104.8 million for the years ended December 31, 2008 and 2007, respectively. The increase in net interest income for 2009 and 2008, was related to both an increase in the average volume of earning assets driven by new commercial loan originations and lower interest rates charged by other business segments due to the decline in short-term interest rates that more than offset lower loan yields due to the significant increase in non-accrual loans and to the repricing at lower rates. However, the Corporation is actively increasing spreads on variable-rate commercial loan renewals given the current market environment. During 2009, the Corporation increased the use of interest rate floors in new commercial and construction loan agreements and renewals to protect net interest margins going forward. The increase in volume of earning assets was primarily due to credit facilities extended to the Puerto Rico Government and its political subdivisions. As of December 31, 2009, the Corporation had \$1.2 billion outstanding of credit facilities granted to the Puerto Rico Government and its political subdivisions.

The provision for loan losses for 2009 was \$273.8 million compared to \$35.5 million and \$12.5 million for 2008 and 2007, respectively. The increase in the provision for loan and lease losses for 2009 was mainly driven by the continuing pressures of a weak Puerto Rico economy and a stagnant housing market that were the main reasons for the increase in non-accrual loans, the migration of loans to higher risk categories (including a significant increase in impaired loans) and the increase in charge-offs. These have resulted in higher specific reserves for impaired loans and increases in loss factors used for the determination of the general reserve. Refer to the *Provision for Loan and Lease Losses* discussion above and to the *Risk Management Allowance for Loan and Lease Losses and Non-performing Assets* discussion below for additional information with respect to the credit quality of the Corporation's commercial and construction loan portfolio. The increase in the provision for loan and lease losses for 2008 was mainly driven by the increase in the amount of commercial and construction impaired loans in Puerto Rico due to deteriorating economic conditions.

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Total non-interest income for the year ended December 31, 2009 amounted to \$5.7 million compared to a non-interest income of \$4.6 million and \$6.2 million for the years ended December 31, 2008 and 2007, respectively. The increase in non-interest income for 2009, as compared to 2008, was mainly attributable to higher non-deferrable loans fees such as agent, commitment and drawing fees from commercial customers. Also, an increase in cash management fees from corporate customers contributed to the increase in non-interest income. The increase in non-interest income for 2008 was mainly attributable to the \$2.5 million gain resulting from an agreement entered into with another local financial institution for the partial extinguishment of secured commercial loans extended to such institution. Aside from this transaction, non-interest income for the Commercial and Corporate Banking Segment increased by \$0.9 million in connection with higher fees on cash management services provided to corporate customers.

Direct non-interest expenses for 2009 were \$41.9 million compared to \$24.5 million and \$20.1 million for 2008 and 2007, respectively. The increase for 2009, as compared to 2008, was primarily due to the portion of the increase in the FDIC deposit insurance premium allocated to this segment; this was partially offset by reductions in compensation expense. The increase for 2008, as compared to 2007, was also mainly due to the portion of the increase in the FDIC insurance premium as increase in compensation and a higher loss in REO operations, primarily due to the increase in the volume of repossessed properties and writedowns.

Mortgage Banking

The Mortgage Banking segment conducts its operations mainly through FirstBank and its mortgage origination subsidiary, FirstMortgage. These operations consist of the origination, sale and servicing of a variety of residential mortgage loans products. Originations are sourced through different channels such as branches, mortgage bankers and real estate brokers, and in association with new project developers. FirstMortgage focuses on originating residential real estate loans, some of which conform to Federal Housing Administration (FHA), Veterans Administration (VA) and Rural Development (RD) standards. Loans originated that meet FHA standards qualify for the federal agency's insurance program whereas loans that meet VA and RD standards are guaranteed by their respective federal agencies. Mortgage loans that do not qualify under these programs are commonly referred to as conventional loans. Conventional real estate loans could be conforming and non-conforming. Conforming loans are residential real estate loans that meet the standards for sale under the FNMA and FHLMC programs whereas loans that do not meet the standards are referred to as non-conforming residential real estate loans. The Corporation's strategy is to penetrate markets by providing customers with a variety of high quality mortgage products to serve their financial needs faster and simpler and at competitive prices.

The Mortgage Banking segment also acquires and sells mortgages in the secondary markets. Residential real estate conforming loans are sold to investors like FNMA and FHLMC. In December 2008, the Corporation obtained from GNMA, Commitment Authority to issue GNMA mortgage-backed securities. Under this program, in 2009, the Corporation securitized and sold FHA/VA mortgage loan production into the secondary markets.

The highlights of the Mortgage Banking segment financial results for the year ended December 31, 2009 include the following:

Segment loss before taxes for the year ended December 31, 2009 was \$14.3 million compared to income of \$8.3 million and \$7.2 million for the years ended December 31, 2008 and 2007, respectively.

Net interest income for the year ended December 31, 2009 was \$39.2 million compared to \$37.3 million and \$27.6 million for the years ended December 31, 2008 and 2007, respectively. The increase in net interest income for 2009 and 2008 was mainly related to the decline in short-term rates. This portfolio is principally composed of fixed-rate residential mortgage loans tied to long-term interest rates that are financed with shorter-term borrowings, thus positively affected in a declining interest rate scenario as the one prevailing in 2009 and 2008. The increase was also related to a higher portfolio, driven in 2009 by the purchase of approximately \$205 million of residential mortgages that previously served as collateral for a commercial loan extended to R&G Financial, a Puerto Rican financial institution. The increase in the portfolio in 2008 was driven by mortgage loan originations.

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The provision for loan and lease losses for the year 2009 was \$29.7 million compared to \$9.0 million and \$1.6 million for the years ended December 31, 2008 and 2007, respectively. The increase in 2009 and 2008 was mainly related to the increase in the volume of non-performing loans due to deteriorating economic conditions in Puerto Rico and an increase in reserve factors to account for the continued recessionary economic conditions and negative loss trends.

Non-interest income for the year ended December 31, 2009 was \$8.5 million compared to \$2.7 million and \$2.1 million for the years ended December 31, 2008 and 2007, respectively. The increase for 2009, as compared to 2008 was driven by approximately \$4.6 million of capitalized servicing assets in connection with the securitization of approximately \$305 million FHA/VA mortgage loans into GNMA MBS. For the first time in several years, the Corporation was engaged in the securitization of mortgage loans throughout 2009. The increase for 2008, as compared to 2007, was driven by a higher volume of loan sales in the secondary market.

Direct non-interest expenses for 2009 were \$32.3 million compared to \$22.7 million and \$20.9 million for 2008 and 2007, respectively. The increase for 2009, as compared to 2008, was also mainly related to the portion of the FDIC deposit insurance premium allocated to this segment, a higher loss on REO operations associated with a higher volume of repossessed properties and an increase in professional service fees. The increase for 2008, as compared to 2007, is related to technology related expenses incurred to improve the servicing of the mortgage loans as well as increases in compensation and, to a lesser extent, higher losses on REO operations in connection with a higher volume of repossessed properties and trends in sales.

Treasury and Investments

The Treasury and Investments segment is responsible for the Corporation's treasury and investment management functions. In the treasury function, which includes funding and liquidity management, this segment sells funds to the Commercial and Corporate Banking, Mortgage Banking, and Consumer (Retail) Banking segments to finance their lending activities and purchases funds gathered by those segments. Funds not gathered by the different business units are obtained by the Treasury Division through wholesale channels, such as brokered deposits, Advances from the FHLB and repurchase agreements with investment securities, among others.

Since the Corporation is a net borrower of funds, the securities portfolio does not result from the investment of excess funds. The securities portfolio is a leverage strategy for the purposes of liquidity management, interest rate management and earnings enhancement.

The interest rates charged or credited by Treasury and Investments are based on market rates.

The highlights of the Treasury and Investments segment financial results for the year ended December 31, 2009 include the following:

Segment income before taxes for the year ended December 31, 2009 amounted to \$163.1 million compared to \$142.3 million for 2008 and of \$36.5 million for the years ended December 31, 2007.

Net interest income for the year ended December 31, 2009 was \$86.1 million compared to \$123.4 million and \$46.5 million for the years ended December 31, 2008 and 2007, respectively. The decrease in 2009, as compared to 2008, was mainly due to the decrease in the amount credited to this segment for its deposit-taking activities due to the decline in interest rates and due to lower yields on investment securities. This was partially offset by reductions in the cost of funding as maturing brokered CDs were replaced with shorter-term CDs at lower prevailing rates and very low-cost sources of funding such as advances from the FED and a higher average volume of investments. Funds obtained through short-term borrowings were invested, in part, in the purchase of investment securities to mitigate the decline in the average yield on securities that resulted from the acceleration of MBS prepayments and calls of U.S. agency debentures (refer to the Financial and Operating Data

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Analysis Investment Activities discussion below for additional information about investment purchases, sales and calls in 2009). The decrease in the yield of investments was driven by the approximately \$945 million of U.S. agency debentures called in 2009 and MBS prepayments. The variance observed in 2008, as compared to 2007, is mainly related to lower short-term rates and, to a lesser extent, to an increase in the volume of average interest-earning assets. The Corporation's securities portfolio is mainly composed of fixed-rate U.S. agency MBS and debt securities tied to long-term rates. During 2008, the Corporation purchased approximately \$3.2 billion in fixed-rate MBS at an average yield of 5.44%, which was significantly higher than the cost of borrowings used to finance the purchase of such assets. Despite the early redemption by counterparties of approximately \$1.2 billion of U.S. agency debentures through call exercises, the lack of liquidity in the financial markets caused several call dates go by in 2008 without issuers actions to exercise call provisions embedded in approximately \$945 million of U.S. agency debentures still held by the Corporation as of December 31, 2008. The Corporation benefited from higher than current market yields on these instruments. Also, non-cash gains from changes in the fair value of derivative instruments and liabilities measured at fair value accounted for approximately \$14.2 million of the increase in net interest income for 2008 as compared to 2007.

Non-interest income for the year ended December 31, 2009 amounted to \$84.4 million compared to income of \$25.6 million and losses of \$2.2 million for the years ended December 31, 2008 and 2007, respectively. The increase in 2009, as compared to 2008, was driven by a \$59.6 million increase in realized gains on the sale of investment securities, primarily reflecting a \$79.9 million gain on the sale of MBS (mainly U.S. agency fixed-rate MBS), compared to realized gains on the sale of MBS of \$17.7 million in 2008. The positive fluctuation in non-interest income for 2008, as compared to 2007, was related to a realized gain of \$17.7 million mainly on the sale of approximately \$526 million of U.S. sponsored agency fixed-rate MBS and to the gain of \$9.3 million on the sale of part of the Corporation's investment in VISA in connection with VISA's IPO. Refer to Non-interest income discussion above for additional information.

Direct non-interest expenses for 2009 were \$7.4 million compared to \$6.7 million and \$7.8 million for 2008 and 2007, respectively. The fluctuations are mainly associated to professional service fees.

United States Operations

The United States operations segment consists of all banking activities conducted by FirstBank in the United States mainland. The Corporation provides a wide range of banking services to individual and corporate customers in the state of Florida through its ten branches and two specialized lending centers. In the United States, the Corporation originally had an agency lending office in Miami, Florida. Then, it acquired Coral Gables-based Ponce General (the parent company of Unibank, a savings and loans bank in 2005) and changed the savings and loan's name to FirstBank Florida. Those two entities were operated separately. In 2009, the Corporation filed an application with the Office of Thrift Supervision to surrender the Miami-based FirstBank Florida charter and merge its assets into FirstBank Puerto Rico, the main subsidiary of First BanCorp. The Corporation placed the entire Florida operation under the control of a new appointed Executive Vice President. The merger allows the Florida operations to benefit by leveraging the capital position of FirstBank Puerto Rico and thereby provide them with the support necessary to grow in the Florida market.

The highlights of the United States operations segment financial results for the year ended December 31, 2009 include the following:

Segment loss before taxes for the year ended December 31, 2009 was \$222.3 million compared to loss of \$62.4 million and \$12.1 million for the years ended December 31, 2008 and 2007, respectively.

Net interest income for the year ended December 31, 2009 was \$2.6 million compared to \$28.8 million and \$38.7 million for the years ended December 31, 2008 and 2007, respectively. The decrease in net interest income for 2009 and 2008 was related to the surge in non-performing assets,

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mainly construction loans, and a decrease in the volume of average earning-assets partially offset by a lower cost of funding due to the decline in market interest rates that benefit interest rates paid on short-term borrowings. In 2009, the Corporation implemented initiatives to accelerate deposit growth with special emphasis on increasing core deposits and shift away from brokered deposits. Also, the Corporation took actions to reduce its non-performing credits including the sales of certain troubled loans.

The provision for loan losses for 2009 was \$188.7 million compared to \$53.4 million and \$30.2 million for 2008 and 2007, respectively. The increase in the provision for loan and lease losses for 2009 was mainly driven by the increase in non-performing loans and the decline in collateral values that has resulted in historical increases in charge-offs levels. Higher delinquency levels and loss trends were accounted for the loss factors used to determine the general reserve. Also, additional charges were necessary because of a higher volume of impaired loans that required specific reserves. Refer to the Provision for Loan and Lease Losses discussion above and to the Risk Management Allowance for Loan and Lease Losses and Non-performing Assets discussion below for additional information with respect to the credit quality of the loan portfolio in the United States. The increase in the provision for loan and lease losses for 2008 was mainly driven by higher specific reserves relating to condo-conversion loans due to the deterioration of the real estate market and a slumping economy.

Total non-interest income for the year ended December 31, 2009 amounted to \$1.5 million compared to a non-interest loss of \$3.6 million and non-interest income of \$1.2 million for the years ended December 31, 2008 and 2007, respectively. The increase in non-interest income for 2009, as compared to 2008, was mainly attributable to a gain of \$0.9 million on the sale of the entire portfolio of auto industry corporate bonds after having taking impairment charges of \$4.2 million on those bonds in 2008. The decrease in non-interest income for 2008 was for the aforementioned impairment charge on corporate bonds and lower service charges on deposit accounts and loan fees.

Direct non-interest expenses for 2009 were \$37.7 million compared to \$34.2 million and \$21.8 million for 2008 and 2007, respectively. The increase for 2009, as compared to 2008, was primarily due to the increase in the FDIC deposit insurance premium, and professional service fees. The increase for 2008, as compared to 2007, was mainly due to a higher loss in REO operations, primarily due to write-downs and expenses related to condo-conversion projects.

Virgin Islands Operations

The Virgin Islands operations segment consists of all banking activities conducted by FirstBank in the U.S. and British Virgin Islands, including retail and commercial banking services as well as insurance activities. In 2002, after acquiring the Chase Manhattan Bank operations in the Virgin Islands, FirstBank became the largest bank in the Virgin Islands (USVI & BVI), serving St. Thomas, St. Croix, St. John, Tortola and Virgin Gorda, with 16 branches. In 2008, FirstBank acquired the Virgin Island Community Bank (VICB) in St. Croix, increasing its customer base and share in this market. The Virgin Islands operations segment is driven by its consumer and commercial lending and deposit-taking activities. Loans to consumers include auto, boat, lines of credit, personal loans and residential mortgage loans. Deposit products include interest bearing and non-interest bearing checking and savings accounts, Individual Retirement Accounts (IRA) and retail certificates of deposit. Retail deposits gathered through each branch serve as the funding sources for the lending activities.

The highlights of the Virgin Islands operations segment financial results for the year ended December 31, 2009 include the following:

Segment income before taxes for the year ended December 31, 2009 was \$0.8 million compared to \$9.2 million and \$26.3 million for the years ended December 31, 2008 and 2007, respectively.

Net interest income for the year ended December 31, 2009 was \$61.1 million compared to \$60.0 million and \$59.1 million for the years ended December 31, 2008 and 2007, respectively. The

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increase in net interest income was primarily due to the decrease in the cost of funding due to maturing CDs renewed at lower prevailing rates and reductions in rates paid on interest-bearing and savings accounts due to the decline in market interest rates. To a lesser, extent, the increase was also due to a higher volume of commercial loans primarily due to approximately \$79.8 million in credit facilities extended to the U.S. Virgin Islands Government and political subdivisions in 2009. The increase for 2008, compared to 2007, was also driven by a lower cost of funding.

The provision for loan and lease losses for 2009 increased by \$12.7 million compared to the same period in 2008 and increased by \$10.0 million when comparing 2008 with the same period in 2007. The increase in the provision for 2009 was mainly related to the construction and residential and commercial mortgage loans portfolio affected by increases to general reserves to account for higher delinquency levels and a challenging economy. The increase in 2008, compared to 2007, was driven by increases to general reserves for the residential, commercial and commercial mortgage loans portfolio to account for negative trends in the economy. General economic conditions worsened, underscoring the severity of recessionary conditions in the US economy, critically important to the U.S. Virgin Islands as the primary market for visitors, trade and investment.

Non-interest income for the year ended December 31, 2009 was \$10.2 million compared to \$9.8 million and \$12.2 million for the years ended December 31, 2008 and 2007, respectively. The increase for 2009, as compared to 2008, was mainly related to higher service charges on deposit accounts and higher ATM interchange fee income. The decrease for 2008, as compared to 2007, was mainly related to the impact in 2007 of a \$2.8 million gain on the sale of a credit card portfolio. Aside from this transaction, non-interest income increased by \$0.4 million primarily due to higher service charges on deposits and higher credit and debit card interchange fee income.

Direct non-interest expenses for the year ended December 31, 2009 were \$45.4 million compared to \$48.1 million and \$42.4 million for the years ended December 31, 2008 and 2007, respectively. The decrease in direct operating expenses for 2009, as compared to 2008, was primarily due to a decrease in compensation expense, mainly due to headcount, overtime and bonuses reductions. The increase in direct operating expense for 2008, compared to 2007, was mainly due to increases in compensation, depreciation and professional service fees.

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The following table presents an average balance sheet of the Corporation for the following years:

December 31,	2009	2008 (In thousands)	2007
ASSETS			
Interest-earning assets:			
Money market & other short-term investments	\$ 182,205	\$ 286,502	\$ 440,598
Government obligations	1,345,591	1,402,738	2,687,013
Mortgage-backed securities	4,254,044	3,923,423	2,296,855
Corporate bonds	4,769	7,711	7,711
FHLB stock	76,982	65,081	46,291
Equity securities	2,071	3,762	8,133
 Total investments	 5,865,662	 5,689,217	 5,486,601
 Residential mortgage loans	 3,523,576	 3,351,236	 2,914,626
Construction loans	1,590,309	1,485,126	1,467,621
Commercial loans	6,343,635	5,473,716	4,797,440
Finance leases	341,943	373,999	379,510
Consumer loans	1,661,099	1,709,512	1,729,548
 Total loans	 13,460,562	 12,393,589	 11,288,745
 Total interest-earning assets	 19,326,224	 18,082,806	 16,775,346
Total non-interest-earning assets ⁽¹⁾	480,998	425,150	438,861
 Total assets	 \$ 19,807,222	 \$ 18,507,956	 \$ 17,214,207
LIABILITIES AND STOCKHOLDERS EQUITY			
Interest-bearing liabilities:			
Interest-bearing checking accounts	\$ 866,464	\$ 580,572	\$ 443,420
Savings accounts	1,540,473	1,217,730	1,020,399
Certificates of deposit	1,680,325	1,812,957	1,652,430
Brokered CDs	7,300,696	7,671,094	7,639,470
 Interest-bearing deposits	 11,387,958	 11,282,353	 10,755,719
Loans payable ⁽²⁾	643,618	10,792	
Other borrowed funds	3,745,980	3,864,189	3,449,492
FHLB advances	1,322,136	1,120,782	723,596
 Total interest-bearing liabilities	 17,099,692	 16,278,116	 14,928,807
Total non-interest-bearing liabilities ⁽³⁾	852,943	796,476	959,361

Total liabilities	17,952,635	17,074,592	15,888,168
Stockholders' equity:			
Preferred stock	909,274	550,100	550,100
Common stockholders' equity	945,313	883,264	775,939
Stockholders' equity	1,854,587	1,433,364	1,326,039
Total liabilities and stockholders' equity	\$ 19,807,222	\$ 18,507,956	\$ 17,214,207

(1) Includes the allowance for loan and lease losses and the valuation on investment securities available-for-sale.

(2) Consists of short-term borrowings under the FED Discount Window Program.

(3) Includes changes in fair value of liabilities elected to be measured at fair value .

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The Corporation's total average assets were \$19.8 billion and \$18.5 billion as of December 31, 2009 and 2008, respectively, an increase for 2009 of \$1.3 billion or 7% as compared to 2008. The increase in average assets was due to: (i) an increase of \$1.1 billion in average loans driven by new originations, in particular credit facilities extended to the Puerto Rico Government and its political subdivisions, and (ii) an increase of \$176.4 million in investment securities mainly due to the purchase of approximately \$2.8 billion in investment securities in 2009 (mainly U.S. agency callable debt securities and U.S. agency MBS) and the securitization of approximately \$305 million FHA/VA loans into GNMA MBS, partially offset by \$1.9 billion in investment securities sold during the year (mainly U.S. agency MBS, including \$452 million in the last month of the year) and \$955 million debt securities called during the year (mainly U.S. agency debentures). The increase in average assets for 2008, as compared to 2007, was also driven by an increase of \$1.1 billion in average loans due to loan originations, mainly commercial and residential mortgage loans, and an increase of \$202.6 million in investment securities, mainly due to purchases of U.S. agency MBS.

The Corporation's total average liabilities were \$18.0 billion and \$17.1 billion as of December 31, 2009 and 2008, respectively, an increase of \$878.0 million or 5% as compared to 2008. The Corporation has diversified its sources of borrowings including: (i) an increase of \$834.2 million in the average balance of advances from the FED and the FHLB, as the Corporation used low-cost sources of funding to match an investment portfolio with a shorter maturity, and (ii) an increase of \$105.6 million in average interest-bearing deposits, reflecting increases in core deposits, mainly in money market accounts in Florida. The Corporation's total average liabilities were \$17.1 billion and \$15.9 billion as of December 31, 2008 and 2007, respectively, an increase of \$1.2 billion or 7% as compared to 2007. The Corporation diversified its sources of borrowings including: (i) an increase of \$526.6 million in average interest-bearing deposits, reflecting increases in brokered CDs used to finance lending activities and to increase liquidity levels as a precautionary measure given the volatile economic climate, and increases in deposits from individual, commercial and government sectors, (ii) an increase of \$414.7 million in alternative sources such as repurchase agreements that financed the increase in investment securities, and (iii) a combined increase of approximately \$408.0 million in advances from FHLB and short-term borrowings from the FED through the Discount Window Program as the Corporation took direct actions to enhance its liquidity position due to the financial market disruptions and to increase its borrowing capacity with the FHLB and the FED, which funds are also used to finance the Corporation's lending activities.

Assets

Total assets as of December 31, 2009 amounted to \$19.6 billion, an increase of \$137.2 million compared to \$19.5 billion as of December 31, 2008. The Corporation's loan portfolio increased by \$860.9 million (before the allowance for loan and lease losses), driven by new originations, mainly credit facilities extended to the Puerto Rico Government and/or its political subdivisions. Also, an increase of \$298.4 million in cash and cash equivalents contributed to the increase in total assets, as the Corporation improved its liquidity position as a precautionary measure given current volatile market conditions. Partially offsetting the increase in loans and liquid assets was a \$790.8 million decrease in investment securities, driven by sales and principal repayments of MBS as well as U.S. agency debt securities called during 2009.

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The following table presents the composition of the loan portfolio including loans held for sale as of year-end for each of the last five years.

<i>(In thousands)</i>	2009	2008	2007	2006	2005
Residential mortgage loans, including loans held for sale	\$ 3,616,283	\$ 3,491,728	\$ 3,164,421	\$ 2,772,630	\$ 2,346,945
Commercial loans:					
Commercial mortgage loans	1,590,821	1,535,758	1,279,251	1,215,040	1,090,193
Construction loans	1,492,589	1,526,995	1,454,644	1,511,608	1,137,118
Commercial and Industrial loans	5,029,907	3,857,728	3,231,126	2,698,141	2,421,219
Loans to local financial institutions collateralized by real estate mortgages and pass-through trust certificates	321,522	567,720	624,597	932,013	3,676,314
Total commercial loans	8,434,839	7,488,201	6,589,618	6,356,802	8,324,844
Finance leases	318,504	363,883	378,556	361,631	280,571
Consumer loans and other loans	1,579,600	1,744,480	1,667,151	1,772,917	1,733,569
Total loans, gross	13,949,226	13,088,292	11,799,746	11,263,980	12,685,929
Less:					
Allowance for loan and lease losses	(528,120)	(281,526)	(190,168)	(158,296)	(147,999)
Total loans, net	\$ 13,421,106	\$ 12,806,766	\$ 11,609,578	\$ 11,105,684	\$ 12,537,930

Lending Activities

As of December 31, 2009, the Corporation's total loans increased by \$860.9 million, when compared with the balance as of December 31, 2008. The increase in the Corporation's total loans primarily relates to increases in C&I loans driven by internal loan originations, mainly to the Puerto Rico Government as further discussed below, partially offset by repayments and charge-offs of approximately \$333.3 million recorded in 2009, mainly for construction loans in Florida.

As shown in the table above, the 2009 loan portfolio was comprised of commercial (60%), residential real estate (26%), and consumer and finance leases (14%). Of the total gross loan portfolio of \$13.9 billion as of December 31, 2009, approximately 83% have credit risk concentration in Puerto Rico, 9% in the United States and 8% in the Virgin Islands, as shown in the following table.

As of December 31, 2009	Puerto Rico	Virgin Islands	United States	Total
	(In thousands)			
Residential real estate loans, including loans held for sale	\$ 2,790,829	\$ 450,649	\$ 374,805	\$ 3,616,283
Commercial mortgage loans	983,125	73,114	534,582	1,590,821
Construction loans (1)	998,235	194,813	299,541	1,492,589
Commercial and Industrial loans	4,756,297	241,497	32,113	5,029,907
Loans to a local financial institution collateralized by real estate mortgages	321,522			321,522
Total commercial loans	7,059,179	509,424	866,236	8,434,839
Finance leases	318,504			318,504
Consumer loans	1,446,354	98,418	34,828	1,579,600
Total loans, gross	\$ 11,614,866	\$ 1,058,491	\$ 1,275,869	\$ 13,949,226
Allowance for loan and lease losses	(410,714)	(27,502)	(89,904)	(528,120)
	\$ 11,204,152	\$ 1,030,989	\$ 1,185,965	\$ 13,421,106

(1) Construction loans of Florida operations include approximately \$70.4 million of condo-conversion loans, net of charge-offs of \$32.4 million.

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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. For purpose of the following presentation, the Corporation separately presented secured commercial loans to local financial institutions because it believes this approach provides a better representation of the Corporation's commercial production capacity.

The following table sets forth certain additional data (including loan production) related to the Corporation's loan portfolio net of the allowance for loan and lease losses for the dates indicated:

	For the Year Ended December 31,				
	2009	2008	2007	2006	2005
	(In thousands)				
Beginning balance	\$ 12,806,766	\$ 11,609,578	\$ 11,105,684	\$ 12,537,930	\$ 9,556,958
Residential real estate loans originated and purchased	591,889	690,365	715,203	908,846	1,372,490
Construction loans originated and purchased	433,493	475,834	678,004	961,746	1,061,773
C&I and Commercial mortgage loans originated and purchased	3,153,278	2,175,395	1,898,157	2,031,629	2,258,558
Secured commercial loans disbursed to local financial institutions					