FIRST BANCORP /PR/
Form 10-K
March 16, 2018

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

FORM 10-K

(Mark one)

[X] **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Fiscal Year Ended December 31, 2017

or

[ ] **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ___________________ to ___________________

Commission File Number 1-14793

FIRST BANCORP.

(Exact name of registrant as specified in its charter)

Puerto Rico	**66-0561882**
(State or other jurisdiction of	(I.R.S. Employer

incorporation or organization)	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:

Common Stock ($0.10 par value)	**New York Stock Exchange**

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

7.125% Noncumulative Perpetual Monthly Income Preferred Stock, Series A (CUSIP: 318672201);

8.35% Noncumulative Perpetual Monthly Income Preferred Stock, Series B (CUSIP: 318672300);

7.40% Noncumulative Perpetual Monthly Income Preferred Stock, Series C (CUSIP: 318672409);

7.25% Noncumulative Perpetual Monthly Income Preferred Stock, Series D (CUSIP: 318672508); and

7.00% Noncumulative Perpetual Monthly Income Preferred Stock, Series E (CUSIP: 318672607)

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company
	Emerging growth company

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

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, 2017 (the last trading day of the registrant's most recently completed second fiscal quarter) was $914,194,471 based on the closing price of $5.79 per share of the registrant's common stock on the New York Stock Exchange on June 30, 2017. The registrant had no nonvoting common equity outstanding as of June 30, 2017. For the purposes of the foregoing calculation only, the registrant has defined affiliates to include (a) the executive officers named in Part III of this Annual Report on Form 10-K; (b) all directors of the registrant; and (c) each shareholder, including the registrant's employee benefit plans but excluding shareholders that file on Schedule 13G, known to the registrant to be the beneficial owner of 5% or more of the outstanding shares of common stock of the registrant as of June 30, 2017. 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: 216,334,736 shares as of February 16, 2018.

Documents incorporated by reference: Portions of the definitive proxy statement relating to the registrant's annual meeting of stockholders scheduled to be held on May 24, 2018 are incorporated by reference in this Form 10-K in response to items 10, 11, 12, 13 and 14 of Part III.

FIRST BANCORP.
2017 ANNUAL REPORT ON FORM 10-K

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SIGNATURES

Forward Looking Statements

This Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), which are subject to the safe harbor created by such sections. When used in this Form 10-K or future filings by First BanCorp. (the “Corporation”) with the U.S. 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 words or phrases “would,” “intends,” “will likely result,” “expect,” “should,” “anticipate,” “look forward,” “believes,” and other terms of similar meaning or import in connection with any discussion of future operating, financial or other performance are 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 to advise readers that these forward-looking statements are not guarantees of future performance and involve certain risks, uncertainties, estimates, and assumptions by us that are difficult to predict. Various factors, some of which are beyond our control, could cause actual results to differ materially from those expressed in, or implied by, such forward-looking statements.

The two hurricanes that affected the Corporation’s service area during the third quarter of 2017 are discussed below in Note 2 to the audited financial statements, in various sections of “Management's Discussion and Analysis of Financial Condition and Results of Operations,” and in Part I, Item 1A, “Risk Factors.” There is pervasive uncertainty surrounding the future economic conditions that will emerge in the storm-affected areas. As a consequence, estimates of the financial impact of these disasters on the Corporation are subject to greater uncertainty than is inherent in other forward-looking statements. The more significant estimates are included in the discussion of the provision for loan and lease losses and the discussion of casualty and disaster response costs and related insurance coverages.

These forward-looking statements include, but are not limited to, the risks described or referenced below in Item 1A. “Risk Factors,” which include the following:

- the actual pace and magnitude of economic recovery in the regions affected by the two hurricanes that affected the Corporation’s service areas during 2017 compared to Management’s current views on the economic recovery;

- uncertainties about how and when rebuilding will take place in the regions affected by the recent storms, including the rebuilding of the public infrastructure, such as Puerto Rico’s power grid, how and when government, private or philanthropic funds will be invested in the affected communities, how many displaced individuals will return to their homes in both the short- and long-term, and what other demographic changes will take place, if any;

- uncertainty as to the ultimate outcomes of actions taken, or those that may be taken, by the Puerto Rico government, or the oversight board established by the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") to address Puerto Rico's financial problems, including the filing of a form of bankruptcy under Title III of PROMESA that provides a court debt restructuring process similar to U.S. bankruptcy protection and the effect of measures included in the Puerto Rico government fiscal plan, or any revisions to it, on our clients and loan portfolios;

- the ability of the Puerto Rico government or any of its public corporations or other instrumentalities to repay its respective debt obligations, including the effect of payment defaults on the Puerto Rico government general obligations, bonds of the Government Development Bank for Puerto Rico (the "GDB") and certain bonds of government public corporations, and recent and any future downgrades of the long-term and short-term debt ratings of the Puerto Rico government, which could exacerbate Puerto Rico's adverse economic conditions and, in turn, further adversely impact the Corporation;

- uncertainty about whether the Federal Reserve Bank of New York (the "New York FED" or "Federal Reserve") will provide approvals for receiving dividends from FirstBank Puerto Rico ("FirstBank" or the "Bank"), or for making payments of dividends on non-cumulative perpetual preferred stock, or payments on trust preferred securities or subordinated debt, incurring, increasing or guaranteeing debt or repurchasing any capital securities, despite the consents that have enabled the Corporation to receive quarterly dividends from FirstBank since the second quarter of 2016, to pay quarterly interest payments on the Corporation's subordinated debentures associated with its trust preferred securities since the second quarter of 2016, and to pay monthly dividends on the non-cumulative perpetual preferred stock since December 2016;

- a decrease in demand for the Corporation’s products and services and lower revenues and earnings because of the continued recession in Puerto Rico;

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

- the Corporation’s reliance on brokered CDs to fund operations and provide liquidity;

- the risk of not being able to fulfill the Corporation’s cash obligations or resume paying dividends to the Corporation’s common stockholders in the future due to the Corporation’s need to receive regulatory approvals to declare or pay any dividends and to take dividends or any other form of payment representing a reduction in capital from FirstBank or FirstBank’s failure to generate sufficient cash flow to make a dividend payment to the Corporation;

- the weakness of the real estate markets and of the consumer and commercial sectors and their impact on the credit quality of the Corporation’s loans and other assets, which have contributed and may continue to contribute to, among other things, high levels of non-performing assets, charge-offs and provisions for loan and lease losses, and may subject the Corporation to further risk from loan defaults and foreclosures;

- the ability of FirstBank to realize the benefits of its net deferred tax assets;

- adverse changes in general economic conditions in Puerto Rico, the United States (“U.S.”), the U.S. Virgin Islands (“USVI”), and the British Virgin Islands (“BVI”), including the interest rate environment, market liquidity, housing absorption rates, real estate prices, and disruptions in the U.S. capital markets, which reduced interest margins and affected funding sources, and have affected demand for all of the Corporation’s products and services and reduced the Corporation’s revenues and earnings and the value of the Corporation’s assets, and may continue to have these effects;

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

- the risk that additional portions of the unrealized losses in the Corporation’s investment portfolio are determined to be other-than-temporary, including additional impairments on the Corporation’s remaining $8.0 million of the Puerto Rico government’s debt securities;

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

- changes in the fiscal and monetary policies and regulations of the U.S. federal government and Puerto Rico and other governments, including those determined by the Board of the Governors of the Federal Reserve System (the "Federal Reserve Board"), the New York FED, the Federal Deposit Insurance Corporation (the "FDIC"), government-sponsored housing agencies, and regulators in Puerto Rico, the USVI and the BVI;

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

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

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

- a need to recognize impairments on the Corporation's financial instruments, goodwill and other intangible assets relating to acquisitions;

- the risk that downgrades in the credit ratings of the Corporation’s long-term senior debt will adversely affect the Corporation’s ability to access necessary external funds;

- the impact on the Corporation’s businesses, business practices and results of operations of a potential higher interest rate environment;

- uncertainty as to whether FirstBank will be able to satisfy its regulators regarding, among other things, asset quality, liquidity plans, maintenance of capital levels and compliance with applicable laws, regulations, and related requirements; and

- general competitive factors and industry consolidation.

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

Investors should refer to Item 1A. Risk Factors, in this Annual Report on Form 10-K, for a discussion of such factors and certain risks and uncertainties to which the Corporation is subject.

PART I

First BanCorp., 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” or “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 Corporation was incorporated under the laws of the Commonwealth of Puerto Rico to serve as the bank holding company for FirstBank. The Corporation is a full service provider of financial services and products with operations in Puerto Rico, the U.S., the USVI and the BVI. As of December 31, 2017, the Corporation had total assets of $12.3 billion, total deposits of $9.0 billion, and total stockholders’ equity of $ 1.9 billion.

The Corporation provides a wide range of financial services for retail, commercial and institutional clients. As of December 31, 2017, the Corporation controlled two wholly-owned subsidiaries: FirstBank and FirstBank Insurance Agency, Inc. (“FirstBank Insurance Agency”). FirstBank is a Puerto Rico-chartered commercial bank, and FirstBank Insurance Agency is a Puerto Rico-chartered insurance agency.

FirstBank is subject to the supervision, examination and regulation of both the Office of the Commissioner of Financial Institutions of Puerto Rico (“OCIF”) and the FDIC. Deposits are insured through the FDIC Deposit Insurance Fund. In addition, within FirstBank, the Bank’s USVI operations are subject to regulation and examination by the United States Virgin Islands Banking Board; its BVI operations are subject to regulation by the British Virgin Islands Financial Services Commission; and its operations in the state of Florida are subject to regulation and examination by the Florida Office of Financial Regulation and the FDIC. The Consumer Financial Protection Bureau (“CFPB”) regulates FirstBank’s consumer financial products and services. 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 three offices in Puerto Rico, and two offices in the USVI and the BVI.

As of December 31, 2017, FirstBank conducts its business through its main office located in San Juan, Puerto Rico, 45 banking branches in Puerto Rico, 11 banking branches in the USVI and the BVI, and 11 banking branches in the state of Florida (USA). As of December 31, 2017, FirstBank has 6 wholly owned subsidiaries with operations 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 28 offices in Puerto Rico; First Management of Puerto Rico, a domestic corporation, which holds tax-exempt assets; FirstBank Puerto Rico Securities, Corp., a broker-dealer subsidiary engaged in investment banking activities, such as advisory services, capital raising efforts on behalf of clients and assistance with financial transaction structuring. FirstBank Overseas Corporation, an international banking entity organized under the International Banking Entity Act of Puerto Rico; and two other companies that hold and operate certain other real estate owned ("OREO") properties.

BUSINESS SEGMENTS

The Corporation has six reportable segments: Commercial and Corporate Banking; Consumer (Retail) Banking; Mortgage Banking; Treasury and Investments; United States Operations; and Virgin Islands Operations. These segments are described below as well as in Note 34, *"Segment Information,"* to the consolidated financial statements for the year ended December 31, 2017 included in Item 8 of this Form 10-K.

Commercial and Corporate Banking

The Commercial and Corporate Banking segment consists of the Corporation's lending and other services for large customers represented by specialized and middle-market clients and the public sector. FirstBank has developed expertise in a wide variety of industries. The Commercial and Corporate Banking segment offers commercial loans, including commercial real estate and construction loans, and floor plan financings, as well as other products, such as cash management and business management services. A substantial portion of the commercial and corporate banking portfolio is secured by the underlying value of the real estate collateral and the personal guarantees of the borrowers. This segment also includes the Corporation's broker-dealer activities.

Consumer (Retail) Banking

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

Mortgage Banking

These operations consist of the origination, sale, and servicing of a variety of residential mortgage loan products and related hedging activities. Originations are sourced through different channels such as FirstBank branches and purchases from mortgage bankers, and in association with new project developers. The Mortgage Banking segment focuses on originating residential real estate loans, some of which conform to Federal Housing Administration (the "FHA"), Veterans Administration (the "VA") and Rural Development (the "RD") standards. Loans originated that meet the FHA's standards qualify for the FHA's insurance program whereas loans that meet the standards of the VA and RD are guaranteed by those respective federal agencies.

Mortgage loans that do not qualify under these programs are commonly referred to as conventional loans. Conventional real estate loans can be conforming or 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 those 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 through a faster and simpler process 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. Most of the Corporation's residential mortgage loan portfolio consists of fixed-rate, fully amortizing, full documentation loans. The Corporation has commitment authority to issue Government National Mortgage Association ("GNMA") mortgage-backed securities. Under this program, the Corporation has been selling FHA/VA mortgage loans into the secondary market since 2009.

Treasury and Investments

The Treasury and Investments segment is responsible for the Corporation's treasury and investment management functions. The treasury function, which includes funding and liquidity management, lends funds to the Commercial and Corporate Banking, Mortgage Banking, and the Consumer (Retail) Banking segments to finance their respective lending activities and borrows from those segments. Funds not gathered by the different business units are obtained by the Treasury function through wholesale channels, such as brokered deposits, advances from the Federal Home Loan Bank ("FHLB"), and repurchase agreements involving investment securities, among others.

United States Operations

The United States Operations segment consists of all banking activities conducted by FirstBank on the United States mainland. FirstBank provides a wide range of banking services to individual and corporate customers primarily in southern Florida through 11 banking branches. The United States Operations segment offers an array of both consumer and commercial banking products and services. Consumer banking products include checking, savings and money market accounts, retail CDs, internet banking services, residential mortgages, home equity loans, lines of credit, and automobile loans. Retail deposits, as well as FHLB advances and brokered CDs assigned to this operation, serve as funding sources for its lending activities. Deposits gathered through FirstBank's branches in the United States also serve as one of the funding sources for lending and investment activities in Puerto Rico.

The commercial banking services include checking, savings and money market accounts, retail CDs, internet banking services, cash management services, remote data capture, and automated clearing house, or ACH, transactions. Loan products include the traditional commercial and industrial and commercial real estate products, such as lines of credit, term loans and construction loans.

Virgin Islands Operations

The Virgin Islands Operations segment consists of all banking activities conducted by FirstBank in the USVI and the BVI, including retail and commercial banking services, with a total of 11 banking branches serving the islands in the USVI of St. Thomas, St. Croix, and St. John, and the island of Tortola in the BVI. The Virgin Islands Operations segment is driven by its consumer, commercial lending and deposit-taking activities.

Loans to consumers include auto, boat, lines of credit, and personal and residential mortgage loans. Deposit products include interest-bearing and non-interest bearing checking and savings accounts, IRAs, and retail CDs. Retail deposits gathered through each branch serve as the funding sources for its own lending activities.

Employees

As of February 1, 2018, the Corporation and its subsidiaries had 2,553 full-time equivalent employees. None of its employees is represented by a collective bargaining group. The Corporation considers its employee relations to be good.

SIGNIFICANT EVENTS SINCE THE BEGINNING OF 2017

Sale of the Puerto Rico Electric Power Authority (“PREPA”) Loan

During the first quarter of 2017, the Corporation received an unsolicited offer for, and sold, its outstanding participation in the PREPA line of credit with a book value of $64 million at the time of sale (principal balance of $75 million), thereby reducing its direct exposure to the Puerto Rico government. A specific reserve of approximately $10.2 million had been allocated to this loan. Gross proceeds from the sale of $53.2 million resulted in an incremental loss of $0.6 million recorded as a charge to the provision for loan and lease losses in 2017.

Sale of Puerto Rico Government available-for-sale debt securities

During the second quarter of 2017, the Corporation sold for an aggregate of $23.4 million three Puerto Rico Government available-for-sale debt securities, specifically bonds of the GDB and the Puerto Rico Public Buildings

Authority, carried on its book at an amortized cost at the time of sale of $23.0 million (net of $34.4 million in cumulative other-than-temporary impairment (“OTTI”) charges). This transaction resulted in a $0.4 million recovery from previous OTTI charges reflected in the statement of income as part of “net gain on sale of investments.” Approximately $12.2 million of the cumulative OTTI charges on these securities was recorded in the first quarter of 2017.

The OTTI charges recorded on Puerto Rico government debt securities considered the latest available information about the Puerto Rico government’s financial condition, including but not limited to credit rating downgrades, revised estimates of recovery rates, and other relevant developments such as government actions, including debt exchange proposals, and the fiscal plan published by the Puerto Rico government in March 2017, as applicable. The Corporation applied a discounted cash flow analysis to its Puerto Rico government debt securities in order to calculate the cash flows expected to be collected and to determine if any portion of the decline in market value of these securities was considered a credit-related OTTI.

U.S Department of Treasury sale of the Corporation’s common stock

On May 10, 2017, the U.S. Department of the Treasury announced that it had sold all of its remaining 10,291,553 shares of the Corporation’s common stock. Since the U.S. Treasury did not recover the full amount of its original investment under the Troubled Asset Relief Program (“TARP”), the senior officers forfeited 2,370,571 of their outstanding shares of restricted stock, resulting in a reduction in the number of the Corporation’s outstanding shares of common stock. The U.S. Treasury continues to hold a warrant to purchase 1,285,899 shares of the Corporation’s common stock.

Natural disasters affecting First BanCorp.

Two strong hurricanes affected the Corporation's service areas during 2017. Early in September, Hurricane Irma, a Category 5 hurricane, affected the eastern Caribbean islands, including the U.S. Virgin Islands of St. Thomas and St. John and Tortola in the British Virgin Islands, and, to a lesser extent, the U.S. Virgin Island of St. Croix and Puerto Rico. After hitting the eastern Caribbean, Hurricane Irma made landfall along Florida's southwest shoreline. Two weeks after Hurricane Irma sideswiped Puerto Rico, Hurricane Maria made landfall in the south-east corner of Puerto Rico as a Category 4 hurricane and exited on the northern coast at a point between the cities of Arecibo and Barceloneta after battering other islands in the Caribbean, including St. Croix. These hurricanes caused widespread property damage, flooding, power outages, and water and communication services interruptions, and have severely disrupted normal economic activity in all of these regions.

As of the end of the third quarter of 2017, the Corporation established a $66.5 million allowance for loan and lease losses directly related to the initial estimate, based on available information, of inherent losses resulting from the impact of the storms. During the fourth quarter of 2017, loan officers performed reviews of the storms' impact on large commercial borrowers, and the results of these reviews were factored into the determination of the allowance for loan and lease losses as of December 31, 2017. The Corporation recorded an incremental provision expense of $4.8 million during the fourth quarter of 2017, primarily related to higher than initial estimated losses associated with the effects of the hurricanes on its commercial and construction loan portfolios. The storm-related allowance as of December 31, 2017 amounted to $68.5 million (net of a $2.8 million charge off taken on a storm-impacted credit during the fourth quarter of 2017). The Corporation's approach to estimating the storms' impact on credit quality is presented in Note 10, *"Allowance for Loan and Lease Losses,"* to the consolidated financial statements included in Item 8 of this Form 10-K.

Interruptions in regular collection efforts caused by Hurricanes Irma and Maria adversely affected the Corporation's non-performing loan statistics. Non-performing residential mortgage loans increased in the second half of 2017 by $23.0 million to $178.3 million as of December 31, 2017 and non-performing commercial and construction loans held for investment increased in the second half of 2017 by $59.4 million to $294.4 million as of December 31, 2017.

In working with borrowers in the Virgin Islands and Puerto Rico affected by Hurricanes Irma and Maria, the Corporation provided three-month deferred repayment arrangements to consumer borrowers (i.e., personal loans, auto loans, finance leases and credit cards) who were current in their payments or no more than two payments in arrears as of the date of the respective hurricane. For residential mortgage loans, the Corporation entered during the third and fourth quarters of 2017 into deferred repayment arrangements on 9,588 residential mortgages totaling $1.3 billion as of December 31, 2017 that provided for a three-month payment deferral for those loans current or no more than two payment in arrears as of the date of the event. For both consumer and residential mortgage loans subject to the deferral programs, each borrower is required to begin making their regularly scheduled loan payment at the end of the deferral period (January 2018) and the deferred amounts were moved to the end of the loan. The payment deferral programs were applied prospectively from the respective dates of the events and did not change the delinquency status of the loans as of such dates. Accordingly, if all payments were current at the date of the event, the loan will not be reported as past due during the deferral period. Furthermore, for loans subject to the deferral programs on which payments were past due prior to the event, the delinquency status of such loans was frozen to the status that existed at the date of the event until the end of the deferral period (January 2018). For commercial and construction loans, the Corporation, on a case by case basis, entered into three-month deferral arrangements for the payment of principal. The Corporation entered into deferral programs related to 351 commercial and construction loans totaling $1.2 billion, with customers that were current in their payments at the date of the event. As of December 31, 2017, residential mortgage and commercial and construction loans in early delinquency (i.e., 30-89 days past due as defined in regulatory report instructions) include $95.1 million and $3.2 million, respectively, of loans subject to the storm-related deferral programs established in Puerto Rico and the Virgin Islands.

Early delinquency figures for residential mortgage loans showed improvements after the end of the deferral period in January 2018 as a substantial amount of residential mortgage customers resumed making their scheduled payments. Residential mortgage loans in early delinquency as of January 31, 2018 amounted to $65.6 million, a $50.3 million decrease, compared to the $115.9 million level as of December 31, 2017, while non-performing residential mortgage loans totaling $177.0 million as of January 31, 2018 remained relatively flat compared to $178.3 million as of December 31, 2017.

With respect to consumer loans, loans in early delinquency as of January 31, 2018 amounted to $65.5 million, a $45.7 million decrease, compared to $111.2 million as of December 31, 2017, while non-performing consumer loans totaling $20.4 million as of January 31, 2018, increased by $3.6 million, as compared to $16.8 million as of December 31, 2017.

For commercial and construction loans, loans in early delinquency as of January 31, 2018 amounted to $31.0 million, a $13.3 million increase compared to $17.6 million as of December 31, 2017, while non-performing commercial and construction loans totaling $292.7 million as of January 31, 2018, decreased $1.8 million, as compared to $294.4 million as of December 31, 2017.

The Corporation implemented its disaster response plan as these hurricanes approached its service areas. To operate in disaster response mode, the Corporation incurred expenses for, among other things, buying diesel fuel and generators for electric power, debris removal, security matters, and emergency communications with customers regarding the status of Bank operations. The disaster response plan costs, combined with payroll and rental costs during the idle time caused by the hurricanes, totaled $6.6 million as of December 31, 2017. Also, certain of the Corporation's facilities and their contents were damaged by these hurricanes. The Corporation has recognized asset impairments of approximately $0.6 million as of December 31, 2017.

The Corporation maintains insurance for casualty losses as well as for disaster response costs and certain revenue lost through business interruption. Management believes, based on its understanding of the insurance coverages, that recovery of $4.8 million of the $7.2 million above-mentioned costs and asset impairments identified as of December 31, 2017 is probable. Accordingly, as of December 31, 2017, a receivable of $4.8 million was included in the audited consolidated statement of financial condition as part of "Other assets" for the expected recovery. Non-interest expenses for 2017 reflect approximately $2.5 million of insurance deductibles related to damages assessed on certain OREO properties and estimated storm-related costs not recoverable under insurance policies.

The Corporation experienced rapid accumulation of deposits after the hurricanes. Total deposits as of December 31, 2017, excluding brokered CDs, increased by $361.5 million from September 30, 2017. The most significant increase was in noninterest-bearing demand deposits, which grew 16%, or $247.5 million, during the fourth quarter of 2017. Storm-related factors, such as the effect of the payment deferral programs and disaster relief funds, contributed to this accumulation. Although management expects the balances accumulated by deposit customers in the storm-affected areas to reduce over time, it is difficult to predict when and to what degree, and there may be some further growth as insurance claims are resolved and additional disaster-recovery funds are distributed. Funds from the deposit build-up were primarily deposited at the Federal Reserve Bank, pending better information on the volatility of these funds.

The Corporation continued normalizing its operations after the hurricanes and its operations have now substantially returned to pre-hurricane levels. As of the date of the filing of this report, 45 out of 48 FirstBank banking branches in Puerto Rico are providing services and connected to the electrical grid, 94% of our network In addition, 82 of our ATMs are operational, 98% of our network, plus 82 of the ATMs that are offered through a third party alliance. Certain of the Corporation's facilities and their contents were damaged by these hurricanes and some of the reopened facilities require the replacements of equipment and furnishings. The Corporation has recognized asset impairments of approximately $0.6 million as of December 31, 2017.

Secondary Offerings of the Corporation's common stock

A secondary offering of the Corporation's common stock by certain of the Corporation's existing stockholders was completed on February 7, 2017. Funds affiliated with Thomas H. Lee Partners, L.P. ("THL") and funds managed by Oaktree Capital Management, L.P. ("Oaktree") sold 20 million shares (10 million shares each) of the Corporation's common stock. Subsequently, the underwriters exercised their option to purchase an additional 3 million shares of the Corporation's common stock from the selling stockholders. In addition, on August 3, 2017, THL and Oaktree participated in another secondary offering of the Corporation's common stock in which they sold an aggregate of 20 million shares (10 million shares each) of common stock. The Corporation did not receive any proceeds from these offerings, and costs incurred in connection with these transactions amounted to $0.4 million in 2017. As of December 31, 2017, each of THL and Oaktree owned less than 5% of the Corporation's common stock. As a result, the directors on the Corporation's Board of Directors who represented THL and Oaktree resigned as directors in August 2017 and the Board appointed Mr. John A. Heffern as a director on October 26, 2017.

Repurchase of Trust Preferred Securities and Dividend Payments on Trust Preferred Securities and Preferred Stock

During the third quarter of 2017, the Corporation completed the repurchase of $7.3 million of trust-preferred securities of the FBP Statutory Trust I that were offered to the Corporation by an investment banking firm. The Corporation repurchased and cancelled the repurchased trust-preferred securities, resulting in a commensurate reduction in the related outstanding amount of the Floating Rate Junior Subordinated Debentures. The Corporation's purchase price equated to 81% of the $7.3 million par value. The 19% discount, plus accrued interest, resulted in a gain of approximately $1.4 million, which is reflected in the consolidated statements of income as a "Gain on early extinguishment of debt."

Written Agreement termination

On October 3, 2017, the New York FED terminated the formal written agreement (the "Written Agreement") entered into on June 3, 2010 by the Corporation and the New York FED. However, the Corporation has agreed with its regulators to continue to obtain approval before paying dividends, receiving dividends from the Bank, making payments on subordinated debt or trust preferred securities, incurring or guaranteeing debt or purchasing or redeeming any corporate stock.

Puerto Rico Government Fiscal Situation, Government Actions, and the Effect of Hurricanes Maria and Irma

A significant portion of our financial activities and credit exposure is concentrated in the Commonwealth of Puerto Rico, which has been in an economic recession since 2006, exacerbated by the effect of Hurricanes Irma and Maria in 2017. Based on the most recent information available included in the new fiscal plan submitted by the Puerto Rico government (the "Revised Fiscal Plan") for the review of the PROMESA oversight board, Puerto Rico's real gross national product ("GNP") has shrunk by more than 14% since 2006. For fiscal year 2018, the Puerto Rico government projects a contraction in the Puerto Rico's GNP of 11.0%, followed by projected growths of 8.4% and 3.5% for fiscal years 2019 and 2020, respectively, based on an assumption of Puerto Rico's receipt of $49.1 billion of Federal Disaster Relief assistance and $21 billion from private insurance funds for recovery and rebuilding efforts after the hurricanes. Meanwhile, the GDB-Economic Activity Index (the "GDB-EAI") in December 2017 was 104.9, a 14.0% reduction compared to December 2016, and a decrease of 13.3% compared to August 2017. The GDB-EAI is a coincident index of economic activity for Puerto Rico made up of four indicators (non-farm payroll employment, electric power generation, cement sales and gasoline consumption). The Revised Fiscal Plan states that the hurricanes will create a spike in inflation of 2.1% in fiscal year 2018, with subsequent average increases of about 1.5% over the next six years, until fiscal year 2023.

The seasonally adjusted unemployment rate in Puerto Rico was 10.9% in December 2017, compared to 12.4% in December 2016. However, the Puerto Rico labor force participation rate was 40.9% as of December 2017. The average of the labor force participation rate in Puerto Rico was 45.05% from 1990 until 2017, reaching an all-time high of 49.80% percent in February of 2007 and a record low of 38.6% in October of 2017. Based on information published by the Puerto Rico government, the labor force estimate was 1.1 million people for December 2017, a reduction of 1.6% when compared with December 2016. The Revised Fiscal Plan reflects that a 20% cumulative decline in population is expected over the next six years.

Based on information published by the Puerto Rico Treasury, the net revenues of the Puerto Rico government's General Fund in December 2017 totaled $697.6 million, which was $101.9 million less than in December 2016. The net revenues to the General Fund for the first half of fiscal year ending June 30, 2018 totaled $3,623.1 million, a decrease of $348.0 million, or 8.8%, compared with the previous fiscal year, and, $157.3 million, or 4.3%, below initial estimates for this period. The Revised Fiscal Plan reflects a projected decline in revenues of 19.8% in fiscal year 2018 before increasing 10.2% in fiscal year 2019 and 5.1% in fiscal year 2020. As per the Revised Fiscal Plan, revenues are forecasted to become 3% higher than pre-hurricane levels by fiscal year 2023, in nominal terms.

Prices on most Commonwealth of Puerto Rico securities have decreased over the past months. General obligations with an eight percent coupon and maturing in 2035 traded in January at an average of 25 cents on the dollar, down from as much as 59 cents in September, before the hurricane.

Bankruptcy Filing

On May 3, 2017, the Puerto Rico government and the PROMESA oversight board filed for a form of bankruptcy in the U.S. District court in Puerto Rico under Title III of PROMESA. The Title III provision allows for a court debt restructuring process similar to U.S. bankruptcy protection. On July 2, 2017, the PROMESA oversight board filed for a similar Title III form of bankruptcy in the U.S. District court in Puerto Rico for PREPA. The mediation on Title III cases were postponed after the hurricanes.

GDB liquidation plan

On April 28, 2017, the PROMESA oversight board approved the fiscal plan of the GDB. With its fiscal plan, the GDB prepares a gradual and orderly wind down of its operations over 10 years that seeks to mitigate the impact to its stakeholders and supports their ability to continue delivering essential services and promote economic growth. Separately from the fiscal plan, the PROMESA oversight board noted that Puerto Rico’s Fiscal Agency and Financial Advisory Authority (“FAFAA”) should provide a certification regarding the anticipated impact that reduced GDB distributions to depositors and other potential exposures might have on other government entities with fiscal plans and/or budgets. With respect to the Puerto Rico Tourism Development Fund (“TDF”), the GDB stated in their fiscal plan that the resolution that created the TDF “specifically provides that the GDB shall not be liable for the payment of any of the TDF’s debts of “any nature,” unless expressly guaranteed by the GDB.

On July 14, 2017, the PROMESA oversight board authorized the GDB to pursue the restructuring of its debts under Title VI of PROMESA and conditionally certified the GDB's Restructuring Support Agreement ("RSA") under the relevant provisions of Title VI. The PROMESA oversight board's decision was in response to a request from FAFAA, dated June 30, 2017, in which the agency noted that the proposed restructuring, along with certain related settlements contemplated by the RSA, will result in an efficient wind down of GDB's operations and a comprehensive financial restructuring of GDB's obligations. The RSA provides for the organized and consensual restructuring of a substantial portion of the GDB's liabilities, including the GDB public bonds, deposit claims by municipalities and certain non-public entities and claims under certain GDB-issued letters of credit and guarantees ("Participating Bond Claims"). In exchange for releasing the GDB from liability relating to these claims, the claim-holders will receive new bonds to be issued by a new entity.

Effect of Hurricanes Maria and Irma and measures taken by authorities

During the third quarter of 2017, Hurricanes Irma and Maria affected Puerto Rico causing significant damage to the infrastructure and property. In the aftermath of Hurricane Maria, the National Oceanic and Atmospheric Administration ("NOAA") stated that damages could total $90 billion. The emergency could cause Puerto Rico's central government and some of its instrumentalities to face severe cash shortfalls from lower revenues, higher cost, and delayed or reduced cost-saving measures that had been required by the fiscal plans previously approved early in 2017.

The Puerto Rico government and the PROMESA oversight board requested federal assistance from the United States federal government. Such assistance is intended to provide Puerto Rico with the cash that it will need to operate its core government services and its disaster response effort in the near future. On December 18, 2017, the U.S. House of Representative introduced a bill to provide additional emergency assistance for the recent hurricanes, wildfires in California, and related agriculture losses. The bill totals $81 billion and targets funds to programs to continue relief and recovery efforts in all of the affected communities, including Texas, Florida, California, Louisiana, Puerto Rico and the USVI.

On February 9, 2018, the Puerto Rico Governor and the Resident Commissioner announced an allocation of $16 billion in federal funds for the island's recovery after Hurricane Maria. This appropriation is part of budget legislation approved by the U.S. Congress and signed by the President of the United States on February 9, 2018. Approximately $11.0 billion of the $16.0 billion was allocated to the community development fund, known as the Community Development Block Grant, to repair homes, support local businesses and rebuild infrastructure while mitigating future risks. From this figure, $2.0 billion will be designated to restore and make improvements to the electrical system. In addition, $1.37 billion was approved for emergency assistance and $150 million under the Direct Loan Program to cover cost sharing with the Federal Emergency Management Agency ("FEMA"). In addition to the $16.0 billion, Puerto Rico is also eligible to participate in other programs that could increase aid to the island to more than $45 billion.

Due to protracted economic and revenue disruptions caused by Hurricane Maria, on October 11, 2017, Moody's lowered the credit ratings on $13.3 billion of Puerto Rico's general obligations from Caa3 to Ca. In addition, the bonds issued by the Puerto Rico Sales Tax Financing Corporation ("COFINA") and PRASA were also downgraded from Ca to Caa3. In total, there were eight types of securities affected, which have a combined par value of $31 billion.

On February 12, 2018, FAFAA released the Revised Fiscal Plans for the Commonwealth, after considering the changes and clarifications required by the PROMESA oversight board to a previous draft. The Fiscal Plan includes substantial revisions that the Puerto Rico government has made to the previous fiscal plan, certified on March 13, 2017 (the "March fiscal plan"), to account for the effect of Hurricanes Maria and Irma and to account for a contemplated transformational transaction. The Revised Fiscal plan uses a six-year horizon, projects a six-year cumulative decline in population of 20%, and projects that by the fiscal year 2023 there will be a $3.4 billion surplus, before any debt service is paid, requiring a liquidity facility to provide public services in fiscal year 2018. The March 2017 fiscal plan covered a 10-year period and allocated around $787 million per year for debt service. The Revised Fiscal Plan also includes projected expenses for Title III proceedings, considers an injection of $49 billion in federal relief assistance, and a series of structural reforms in, among other things, the areas of ease of doing business, human capital, tax reform, and power sector reform, including a layout for the privatization of PREPA. The Revised Fiscal Plan also creates an annual reserve of $130 million and a $400 million investment for infrastructure maintenance and development. The PROMESA oversight board is expected to evaluate the plan in the coming weeks and, after public hearing, determine whether to certify it.

Exposure to the Puerto Rico Government

As of December 31, 2017, the Corporation had $214.5 million of direct exposure to the Puerto Rico government, its municipalities and public corporations, compared to $323.3 million as of December 31, 2016. As of December 31, 2017, approximately $184.6 million of the exposure consisted of loans and obligations of municipalities in Puerto Rico that are supported by assigned property tax revenues and for which, in most cases, the good faith, credit and unlimited taxing power of the applicable municipality have been pledged to their repayment. These municipalities are required by law to levy special property taxes in such amounts as are required for the payment of all of their respective general obligation bonds and loans. The PROMESA oversight board has not designated any of Puerto Rico's 78 municipalities as covered entities under PROMESA. However, while the Revised Fiscal Plan did not contemplate a restructuring of the debt of Puerto Rico's municipalities, the plan did call for the gradual elimination of budgetary subsidies provided to municipalities by the central government. Furthermore, municipalities are also likely to be affected by the negative economic and other effects resulting from expense, revenue or cash management measures taken to address the Puerto Rico Government's budgetary and liquidity shortfalls, or measures included in fiscal plans of other government entities, such as the GDB Restructuring Support Agreement. The GDB Restructuring Support Agreement provides for the restructuring of a substantial portion of the GDB's indebtedness, including deposits of municipalities, through the issuance of "Participating Bond Claims" in exchange for the release of the GDB from liability relating to the bonds, deposits, letters of credit and guarantees. In addition to municipalities, the total direct exposure also includes a $6.8 million loan to a unit of the central government and a $15.1 million loan to an affiliate of a public corporation. The Corporation's total direct exposure also includes obligations of the Puerto Rico Government, specifically bonds of the Puerto Rico Housing Finance Authority, at an amortized cost of $8.0 million as part of its available-for-sale investment securities portfolio recorded on its books at a fair value of $6.8 million as of December 31, 2017.

Furthermore, as of December 31, 2017, the Corporation had three commercial mortgage loans granted to the hotel industry in Puerto Rico that were previously guaranteed by the TDF ("TDF commercial mortgage loans") with an outstanding principal balance of $120.2 million (book value of $70.8 million), compared to $127.7 million outstanding (book value of $111.8 million) as of December 31, 2016. Historically, the borrower and the operations of the underlying collateral of these loans have been the primary sources of repayment and the TDF, which is a subsidiary of the GDB, provided a secondary guarantee for payment performance. As part of agreements executed in the second quarter of 2017 and first quarter of 2018, the TDF paid $7.6 million and $4.0 million, respectively, to honor a portion of its guarantee on these loans. As provided in the agreements, the cash payments received by the Corporation released the TDF from its liability as a guarantor of these loans. As a result, the income-producing real estate properties are now the only collateral of such loans, thus, any decline in collateral valuations may require additional impairments on these loans. All the three TDF commercial mortgage loans have been classified as non-performing and impaired since the first quarter of 2016, and interest payments have been applied against principal since then. Approximately $4.7 million of interest payments received on loans guaranteed by the TDF since late March 2016 have been applied against principal. During 2017, the Corporation recorded charge-offs totaling $30.8 million on these facilities for the portion of the recorded investment in excess of the fair value of the collateral and the guarantee, considering the aforementioned agreements reached with the TDF. In addition, GDB agreed to issue to the Bank a fixed income financial instrument pursuant to the GDB's Restructuring Support Agreement approved by the PROMESA oversight board. As of December 31, 2017, the non-performing TDF commercial mortgage loans and related facilities are being carried (net of reserves and accumulated charge-offs) at 52% of the unpaid principal balance.

In addition, the Corporation had $116.5 million in exposure to residential mortgage loans that are guaranteed by the Puerto Rico Housing Finance Authority (the "PRHFA"). Residential mortgage loans guaranteed by the PRHFA are secured by the underlying properties and the guarantees serve to cover shortfalls in collateral in the event of a borrower default. The Puerto Rico government guarantees up to $75 million of the principal under the mortgage loan insurance program. According to the most recently released audited financial statements of the Puerto Rico Housing Financing Authority, as of June 30, 2015, the PRHFA's mortgage loan insurance program covered loans in an aggregate of approximately $552 million. The regulations adopted by the PRHFA require the establishment of adequate reserves to guarantee the solvency of the mortgage loan insurance fund. As of June 30, 2015, the most recent date as to which information is available, the PRHFA had a restricted net position for such purposes of approximately $77.4 million.

As of December 31, 2017, the Corporation had $490.3 million of public sector deposits in Puerto Rico, compared to $408.8 million as of December 31, 2016. As of December 31, 2017, approximately 29% of the public sector deposits in Puerto Rico are from municipalities and municipal agencies and 71% are from public corporations and the central government and agencies.

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 and proxy statements on Schedule 14A, filed or furnished pursuant to section 13(a), 14(a) or 15(d) of the Exchange Act, free of charge on or through its internet website at www.1firstbank.com (under “Investor Relations”), 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 and principles, the charters of the audit, asset/liability, compensation and benefits, credit, compliance, risk, corporate governance and nominating committees and the codes of conduct and independence principles mentioned below, free of charge on or through its internet website at www.1firstbank.com (under “Investor Relations”):

- Code of Ethics for CEO and Senior Financial Officers
- Code of Ethics applicable to all employees
- Corporate Governance Standards
- Independence Principles for Directors
- Luxury Expenditure Policy

The corporate governance guidelines and principles 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.

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, 2017, the Corporation also had a presence in the state of Florida and in the USVI and the BVI.

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 in 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 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

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. Most of the regulations required under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") now have been adopted. Although there is a possibility of additional Dodd-Frank Act-related regulations in the future, the pace of new regulations under the Dodd-Frank Act may abate. In addition, future legislation may increase the regulation and oversight of the Corporation and FirstBank, although it is also possible that future legislation could reduce the regulatory compliance obligations of FirstBank and the Corporation. Any change in applicable laws or regulations, however, may have a material adverse effect on the business of commercial banks and bank holding companies, including FirstBank and the Corporation.

Dodd-Frank Act

The Dodd-Frank Act significantly changed the regulation of financial institutions and the financial services industry. The Dodd-Frank Act includes numerous provisions that have affected and will affect large and small financial institutions alike, including banks and bank holding companies and how they will be regulated in the future. As a result of the Dodd-Frank Act, there has been and will be in the future additional regulatory oversight and supervision of the Corporation and its subsidiaries.

The Dodd-Frank Act, among other things, imposes new capital requirements on bank holding companies; provides that a bank holding company must serve as a source of financial and managerial strength to each of its subsidiary banks and stand ready to commit resources to support each of them; changes the base for FDIC insurance assessments to a bank's average consolidated total assets minus average tangible equity, rather than upon its deposit base, and permanently raises the current standard deposit insurance limit to $250,000; and expands the FDIC's authority to raise insurance premiums. The legislation also calls for the FDIC to raise the ratio of reserves to deposits from 1.15% to 1.35% for deposit insurance purposes by September 30, 2020 and to "offset the effect" of increased assessments on insured depository institutions with assets of less than $10 billion.

The CFPB, which was created by the Dodd-Frank Act, has broad rulemaking, supervisory and enforcement authority over consumer financial products and services, including deposit products, residential mortgages, home-equity loans and credit cards, and contains provisions on mortgage-related matters such as steering incentives and determinations as to a borrower's ability to repay the principal amount and prepayment penalties.

The CFPB has primary examination and enforcement authority over FirstBank and other banks with over $10 billion in assets with respect to consumer financial products and services.

The Dodd-Frank Act also limits interchange fees payable on debit card transactions. The Federal Reserve Board's current debit card interchange rule caps a debit card issuer's base fee at 21 cents per transaction and allows an additional 5 basis-point charge per transaction to help cover fraud losses. The debit card interchange rule has reduced our interchange fee revenue in line with industry-wide expectations since 2011.

The Dodd-Frank Act includes provisions that affect corporate governance and executive compensation at all publicly-traded companies and allows financial institutions to pay interest on business checking accounts. The legislation also restricts proprietary trading, places restrictions on the owning or sponsoring of hedge and private equity funds, and regulates the derivatives activities of banks and their affiliates.

Section 171 of the Dodd-Frank Act (the "Collins Amendment"), among other things, eliminates certain trust-preferred securities from Tier I capital. Preferred securities issued under the U.S. Treasury's Troubled Asset Relief Program

(“TARP”) are exempt from this treatment. Bank holding companies, such as the Corporation, were required to fully phase out these instruments from Tier 1 capital by January 1, 2016; however, these instruments may remain in Tier 2 capital until the instruments are redeemed or mature.

Regulatory Capital and Liquidity Coverage Developments. The federal banking agencies adopted new rules for U.S. banks that revise important aspects of the minimum regulatory capital requirements, the components of regulatory capital, and the risk-based capital treatment of bank assets and off-balance sheet exposures. The final rules, which currently apply to the Corporation and FirstBank, generally are intended to align U.S. regulatory capital requirements with international regulatory capital standards adopted by the Basel Committee on Banking Supervision (“Basel Committee”), in particular the most recent international capital accord adopted in 2010 (and revised in 2011) known as “Basel III.” The current rules increase the quantity and quality of capital required by, among other things, establishing a minimum common equity capital requirement and an additional common equity Tier 1 capital conservation buffer. In addition, the current rules revise and harmonize the bank regulators’ rules for calculating risk-weighted assets to enhance risk sensitivity and address weaknesses that have been identified, by applying a variation of the Basel III “standardized approach” for the risk-weighting of bank assets and off-balance sheet exposures to all U.S. banking organizations other than large internationally active banks.

Consistent with Basel III and the Collins Amendment, the current rules also establish a more conservative standard for including an instrument such as trust-preferred securities as Tier 1 capital for bank holding companies with total consolidated assets of $15 billion or more as of December 31, 2009. Bank holding companies such as the Corporation were required to fully phase out these instruments from Tier I capital by January 1, 2016, although qualifying trust preferred securities may be included as Tier 2 capital until the instruments are redeemed or mature. As of December 31, 2017, the Corporation had $202.4 million in trust preferred securities that are subject to a full phase-out from Tier 1 capital under the final regulatory capital rules discussed above. During the third quarter of 2017, the Corporation completed the repurchase of $7.3 million of trust preferred securities of the FBP Statutory Trust I that were offered to the Corporation by an investment banking firm. This transaction is described in more detail in “Significant Events Since the Beginning of 2017” above.

The current capital rules became effective for the Corporation and our subsidiary bank on a multi-year transitional basis starting on January 1, 2015, and, in general, will be fully effective as of January 1, 2019, although certain elements of the new rules have recently been deferred by the federal banking agencies. The new general minimum regulatory capital requirements and the "standardized approach" for risk weighting of a banking organization's assets, however, currently fully apply to us. The rules have increased our regulatory capital requirements and require us to hold more capital against certain of our assets and off-balance sheet exposures. The Corporation's estimated pro-forma common equity Tier 1 ratio, Tier 1 capital ratio, total capital ratio, and the leverage ratio under the Basel III rules, giving effect as of December 31, 2017 to all the provisions that will be phased-in, were 18.09 %, 18.49 %, 21.99 %, and 14.01 %, respectively. These ratios would exceed the fully phased-in minimum capital ratios under Basel III.

These regulatory capital requirements are discussed in further detail in "Regulation and Supervision – Bank and Bank Holding Company Regulatory Capital Requirements."

International Regulatory Capital and Liquidity Coverage Developments

International regulatory developments can affect the regulation and supervision of U.S. banking organizations, including the Corporation and FirstBank. Both the Basel Committee and the Financial Stability Board (established in April 2009 by the Group of Twenty ("G-20") Finance Ministers and Central Bank Governors) have agreed to take action to strengthen regulation and supervision of the financial system with greater international consistency, cooperation and transparency, including the adoption of Basel III and a commitment to raise capital standards and liquidity buffers within the banking system under Basel III.

In late 2014, the Basel Committee issued its final requirements for a Net Stable Funding Ratio ("NSFR"). The NSFR compares the amount of an institution's available stable funding ("ASF", the ratio's numerator) to its required stable funding ("RSF", the ratio's denominator) to measure how the institution's asset base is funded. ASF is defined as the portion of capital and liabilities expected to be reliable over the time horizon considered by the NSFR, which extends to one year. While the NSFR is intended to be applied to large, internationally active banks, at the discretion of national supervisors it can be applied to other banking organizations or classes of banking organizations. As proposed by the U.S. federal banking agencies in May 2016, however, the NSFR requirements would not apply to the Corporation.

Prudential Regulation Developments. U.S. banking organizations, including the Corporation and FirstBank, operate under the federal banking agencies' rules and general supervisory guidance for stress testing practices applicable to banking organizations with more than $10 billion in total consolidated assets. These regulatory actions require bank holding companies with total consolidated assets of between $10 billion and $50 billion, consistent with the Dodd-Frank Act, to comply with annual company-run stress testing requirements, outline broad principles for a satisfactory stress testing framework, including principles related to governance, controls and use of results, and describe various stress testing approaches and how stress testing should be used at various levels within an organization.

Under these requirements, the Corporation is subject to two stress testing rules that implement provisions of the Dodd-Frank Act, one issued by the Federal Reserve Board that applies to the Corporation on a consolidated basis and one issued by the FDIC that applies to the Bank. These Dodd-Frank Act stress tests are designed to require banking organizations to assess the potential impact of different economic scenarios on their earnings, losses, and capital over a set time period, with consideration given to certain relevant factors, including the organization's condition, risks, exposures, strategies, and activities. The Dodd-Frank Act stress tests require banking organizations with total consolidated assets of more than $10 billion but less than $50 billion, including the Corporation and the Bank, to conduct annual company-run stress tests using certain scenarios that the Federal Reserve Board publishes by February 15 of each year, report the results to their primary federal regulator and the Federal Reserve Board by July 31 of the same year, and publicly disclose a summary of the results by October 31 of that year.

The Federal Reserve Board and the other federal banking agencies have published final supervisory guidance describing their supervisory expectations for the Dodd-Frank Act stress tests to be conducted by financial institutions, including the Corporation and the Bank. The final guidance provides flexibility to accommodate different risk profiles, sizes, business lines, market areas, and complexity approaches for banking institutions in the $10 billion to $50 billion asset range, and provides examples of practices that would be consistent with supervisory expectations. This guidance is fully applicable to the Corporation and the Bank. The final guidance also confirms that banking organizations with assets between $10 billion and $50 billion are not subject to the more extensive capital planning and stress-testing requirements that apply to bank holding companies with assets of at least $50 billion, including the Federal Reserve capital plan rule, the annual Comprehensive Capital Analysis and Review, the Dodd-Frank Act supervisory stress tests, and related data collections. On October 31, 2017, the Corporation released the results of its "company-run" stress test required by the Dodd-Frank Act ("DFAST") for the Corporation and the Bank. The Corporation and the Bank are required to disclose on an annual basis the results of the severely adverse scenario of the DFAST annual capital stress test. Results indicate that, even in the severely adverse scenario presented under the test, the Corporation's capital ratios exceed both the regulatory minimum required ratios mandated under Basel III and the well-capitalized thresholds throughout the nine-quarter planning horizon.

The Federal Reserve's rules that govern the supervision and regulation of large U.S. bank holding companies and foreign banking organizations, as required by the Dodd-Frank Act, generally apply only to institutions with total consolidated assets of $50 billion or more, which would not affect the Corporation. The Federal Reserve's rules, however, require publicly-traded U.S. bank holding companies with total consolidated assets of $10 billion or more, such as the Corporation, to establish enterprise-wide risk committees. These requirements complement the stress testing and resolution planning requirements for large bank holding companies that the Federal Reserve previously finalized. The current rules require the Corporation's risk management framework to be commensurate with the Corporation's structure, risk profile, complexity, activities and size, and must include policies and procedures establishing risk-management governance, risk-management policies, and risk control infrastructure for the Corporation's global operations and processes and systems for implementing and monitoring compliance with such policies and procedures. In addition, one independent director must chair the risk committee, with the banking organization determining the appropriate proportion of independent directors on the committee, based on its size, scope, and complexity, provided that it meets the minimum requirement of one independent director. Also, at least one director with risk-management experience must be appointed to the risk committee. The Corporation is in compliance with these requirements.

Consumer Financial Protection Bureau. CFPB regulations issued over the past few years implement the Dodd-Frank Act amendments to the Equal Credit Opportunity Act, the Truth in Lending Act ("TILA"), and the Real Estate Settlement Procedures Act ("RESPA"). In general, among other changes, these regulations collectively: (i) require lenders to make a reasonable good faith determination of a prospective residential mortgage borrower's ability to repay based on specific underwriting criteria and set standards for mortgage lenders to determine whether a consumer has the ability to repay the mortgage, (ii) require stricter underwriting of "qualified mortgages," discussed below, that presumptively satisfy the ability to pay requirement (thereby providing the lender a safe harbor from non-compliance claims), (iii) specify new limitations on loan originator compensation and establish criteria for the qualifications of, and registration or licensing of loan originators, (iv) further restrict certain high-cost mortgage loans by expanding the coverage of the Home Ownership and Equity Protections Act of 1994, (v) expand mandated loan escrow accounts for certain loans, (vi) revise existing appraisal requirements under the Equal Credit Opportunity Act and require provision of a free copy of all appraisals to applicants for first lien loans, (vii) establish new appraisal standards for most "higher-risk mortgages" under TILA, (viii) combine in a single, new form required loan disclosures under TILA and RESPA, (ix) define a "qualified mortgage" for purposes of the Dodd Frank Act, and (x) afford safe harbor legal protections for lenders making qualified loans that are not "higher priced."

The CFPB also has issued final regulations setting forth new mortgage servicing rules that now apply to the Bank.

The regulations affect notices given to consumers as to delinquency, foreclosure alternatives and loss mitigation, modification applications, interest rate adjustments and options for avoiding "force-placed" insurance. Servicers are prohibited from processing foreclosures when a loan modification is pending, and must wait until a loan is more than 120 days delinquent before initiating a foreclosure action.

The servicer must provide direct and ongoing access to its personnel, and provide prompt review of any loss mitigation application. Servicers must maintain accurate and accessible mortgage records for the life of a loan and until one year after the loan is paid off or transferred.

In October 2016, the CFPB adopted further changes to these mortgage servicing rules. The new changes generally clarify and amend provisions regarding force-placed insurance notices, policies and procedures, early intervention, loss mitigation requirements and periodic statement requirements under the CFPB mortgage servicing rules. The amendments also address proper compliance regarding certain servicing requirements when a consumer is a potential or confirmed successor in interest, is in bankruptcy, or sends a cease communication request under the Fair Debt Collection Practices Act. These amendments became generally effective in October 2017, although provisions relating to bankruptcy periodic statements and successors-in-interest will become effective in April 2018. These new mortgage servicing standards are expected to add to our costs of conducting a mortgage servicing business.

The Dodd-Frank Act direct the Bureau to publish rules and forms that combine certain disclosures that consumers receive in connection with applying for and closing on a mortgage loan under the TILA and the RESPA. Consistent with this requirement, the Bureau has amended Regulation X (Real Estate Settlement Procedures Act) and Regulation Z (Truth in Lending) to establish new disclosure requirements and forms in Regulation Z for most closed-end consumer credit transactions secured by real property. In addition to combining the existing disclosure requirements and implementing new requirements imposed by the Dodd-Frank Act, the rule provides extensive guidance regarding compliance with those requirements.

The Volcker Rule. This section of the Dodd-Frank Act, subject to important exceptions, generally prohibits a banking entity such as the Corporation or FirstBank from acquiring or retaining any ownership in, or acting as sponsor to, a hedge fund or private equity fund ("covered fund"). The Volcker Rule also prohibits these entities from engaging, for their own account, in short-form proprietary trading of certain securities, derivatives, commodity futures and options on these instruments.

Final regulations implementing the Volcker Rule have been adopted by the financial regulatory agencies and are now generally effective.

The Corporation and the Bank are not engaged in proprietary trading as defined in the Volcker Rule. In addition, a review of the Corporation’s investments was undertaken to determine if any meet the Volcker Rule’s definition of covered funds. Based on that review, the Corporation’s investments are not considered covered funds under the Volcker Rule.

Community Reinvestment Act and Home Mortgage Disclosure Act Regulations. The Community Reinvestment Act (“CRA”) encourages banks to help meet the credit needs of the local communities in which the banks offer their services, including low- and moderate-income individuals, consistent with the safe and sound operation of the bank.

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 its most recent examination by the FDIC.

Failure to adequately serve the communities could result in the denial by the regulators to merge, consolidate or acquire new assets, as well as expand or relocate branches.

The federal bank regulatory agencies have amended their respective CRA regulations primarily to conform to changes made by the CFPB to Regulation C, which implements the Home Mortgage Disclosure Act (“HMDA”).

Since 1995, the Federal Reserve Board, the FDIC, and the Office of the Comptroller of the Currency have conformed certain definitions in their respective CRA regulations to the scope of loans reported under Regulation C and believe that continuing to do so produces a less burdensome CRA performance evaluation process. In particular, the agencies have amended their CRA regulations to revise the definitions of "home mortgage loan" and "consumer loan," as well as the public file content requirements. These revisions maintain consistency between the CRA regulations and amendments to Regulation C, which generally became effective on January 1, 2018.

In addition, the final rule contains technical corrections and removes obsolete references to the Neighborhood Stabilization Program.

The amendments to the CRA regulations also became effective on January 1, 2018.

Future Legislation and Regulation. While the federal agencies have adopted regulations that implement many requirements of the Dodd-Frank Act, important regulatory actions (e.g., the adoption of rules regarding the compensation of financial institutions executives) that could have an impact on the Corporation and the Bank remain to be taken. Additional consumer protection laws may be enacted, and the FDIC, Federal Reserve and CFPB have adopted and may adopt in the future new regulations that have addressed or may address, among other things, banks' credit card, overdraft, collection, privacy and mortgage lending practices. Additional consumer protection regulatory activity is possible in the near future. On the other hand, legislation has been introduced in Congress to reduce some of the Dodd-Frank Act's regulatory burdens, including certain provisions relating to enhanced prudential supervision. These changes, if enacted into law, would primarily affect banking organizations of less than $50 billion in assets, including the Corporation and the Bank.

Such proposals and legislation, if finally adopted and implemented, would change banking laws and our operating environment and that of our subsidiaries in ways that could be substantial and unpredictable. We 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 our financial condition or results of operations.

Bank Holding Company Activities and Other Limitations

The Corporation is registered and subject to regulation under the Bank Holding Company Act of 1956, as amended (the "Bank Holding Company Act" or "BHC 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, and assess substantial civil money penalties, against bank holding companies and their non-bank subsidiaries. In addition, 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.

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.

The Bank Holding Company Act also permits a bank holding company to elect to become a financial holding company and engage in a broad range of activities that are financial in nature. The Corporation filed an election with the Federal Reserve Board and became a financial holding company under the Bank Holding Company Act. 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 Bank Holding Company 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) domestic activities permitted for existing bank holding company; (g) foreign activities permitted for existing bank holding company; and (h) merchant banking activities.

A financial holding company that ceases to meet certain standards is subject to a variety of restrictions, depending on the circumstances, including precluding the undertaking of new activities or the acquisition of shares or control of other companies. 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 alternative, to discontinue or divest any activities that are permitted only to non-financial holding company bank holding companies. The Corporation and FirstBank must be well-capitalized and well-managed for regulatory purposes, and FirstBank must earn “satisfactory” or better ratings on its periodic CRA examinations to preserve the financial holding company status. The Corporation currently is restricted in its ability to engage in new activities or the acquisition of shares or control of other companies without the prior written approval of the Board of Governors of the Federal Reserve System.

The potential restrictions are different if the lapse pertains to the CRA. In that case, until all the subsidiary institutions are restored to at least a “satisfactory” CRA rating status, the financial holding company may not engage, directly or through a subsidiary, in any of the additional financial activities permissible under the Bank Holding Company 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 Bank Holding Company Act does not require divestiture for this type of situation.

Under provisions of the Dodd-Frank Act and Federal Reserve Board policy, a bank holding company such as the Corporation is expected to act as a source of financial and managerial 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, 2017, and the date hereof, FirstBank was and is the only depository institution subsidiary of the Corporation. The Dodd-Frank Act directs the Federal Reserve Board to adopt regulations adopting the statutory source-of-strength requirements, but implementing regulations have not yet been proposed.

Emergency Economic Stabilization Act of 2008

Turmoil in the U.S. financial sector during 2008 resulted in the passage of the Emergency Economic Stabilization Act of 2008 (the "EESA") and the adoption of several programs by the U.S. Treasury, as well as several actions by the Federal Reserve Board. The EESA authorized the U.S. 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 TARP was action by the U.S. Treasury to make significant investments in U.S. financial institutions through the Capital Purchase Program ("CPP"). The U.S. 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 U.S. Treasury approved, a capital purchase in the amount of $400,000,000. The Corporation entered into a Letter Agreement, dated as of January 16, 2009, including the Securities Purchase Agreement Standard Terms (collectively the "Letter Agreement") with the U.S. 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 Fixed Rate Cumulative Perpetual Preferred Stock, Series F (the "Series F Preferred Stock"), and (ii) a warrant to purchase 389,483 shares of the Corporation's common stock at an exercise price of

$154.05 per share, subject to certain anti-dilution and other adjustments (the "warrant"). The TARP transaction closed on January 16, 2009. On July 20, 2010, we exchanged the Series F Preferred Stock, plus accrued dividends on the Series F Preferred Stock, for 424,174 shares of a new series of preferred stock, fixed rate Cumulative Mandatorily Convertible Preferred Stock, Series G (the "Series G Preferred Stock"), and amended the warrant. On October 7, 2011, we exercised our right to convert the Series G Preferred Stock into 32,941,797 shares of common stock. As a result of the issuance of $525 million of common stock in October 2011, the warrant was adjusted to provide for the issuance of approximately 1,285,899 shares of common stock at an exercise price of $3.29 per share. On August 16, 2013, a secondary offering of the Corporation's common stock was completed by certain of the Corporation's existing stockholders, which included the sale by the U.S. Treasury of 13 million shares in such secondary offering. In the fourth quarter of 2014, the U.S. Treasury sold an additional 4.4 million shares in accordance with its first pre-defined written trading plan. On May 10, 2017, the U.S. Treasury announced the sale of its remaining 10.3 million shares of First BanCorp.'s common stock. As of December 31, 2017, the U.S. Treasury continues to hold a warrant to purchase 1,285,899 shares of the Corporation's outstanding common stock.

As a result of the U.S. Treasury's sale of all of the Corporation's shares of common stock held by it, the Corporation is no longer subject to the compensation-related restrictions under TARP, which substantially limited the Corporation's ability to award short-term and long-term incentives to the Corporation's executives, and the transferability restrictions on the shares of restricted stock held by the senior officers subject to the restrictions lapsed. However, since the U.S. Treasury did not recover the full amount of its original investment under TARP, 2,370,571 outstanding shares of restricted stock held by senior officers were forfeited, resulting in a reduction in the number of common shares outstanding. If the U.S. Treasury exercises all or part of its warrant to purchase the Corporation's common stock, the compensation-related restrictions of TARP would not be reimposed on the Corporation for the period of time that such common stock was held by the U.S. Treasury.

USA PATRIOT Act and Other Anti-Money Laundering Requirements.

As a regulated depository institution, FirstBank is subject to the Bank Secrecy Act, which imposes a variety of reporting and other requirements, including the requirement to file suspicious activity and currency transaction reports that are designed to assist in the detection and prevention of money laundering and other criminal activities. In addition, under Title III of the USA PATRIOT Act of 2001, 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.

Regulations implementing the Bank Secrecy Act and the USA PATRIOT Act are published and primarily enforced by the Financial Crimes Enforcement Network, a bureau of the U.S. Treasury. Failure of a financial institution to comply with the requirement of the Bank Secrecy Act or the USA PATRIOT Act could have serious legal and reputational consequences for the institution, including the possibility of regulatory enforcement or other legal action, including significant civil money penalties, against the Corporation or the Bank. The Corporation also is required to comply with federal economic and trade sanctions requirements enforced by the Office of Foreign Assets Control ("OFAC"), a bureau of the U.S. Treasury. The Corporation has adopted appropriate policies, procedures and controls to address compliance with the Bank Secrecy Act, USA PATRIOT Act and economic/trade sanctions requirements, and to implement banking agency, U.S. Treasury and OFAC regulations.

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

FirstBank is subject to regulation and examination by the OCIF, the CFPB and the FDIC, and is subject to comprehensive federal and state (Commonwealth) regulations dealing with a wide variety of subjects. The federal and state laws and regulations that 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 and 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.

There are periodic examinations by the OCIF, the CFPB and the FDIC of FirstBank to test the Bank's conformance to safe and sound banking practices and compliance with various statutory and regulatory requirements. This regulation and supervision establishes a comprehensive framework and oversight of activities in which a banking institution can engage. The regulation and supervision by the FDIC are 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, 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.

Written Agreement

FirstBank was notified by the FDIC that the Consent Order under which the Bank had been operating since June 2, 2010 was terminated effective April 29, 2015. FirstBank is required to maintain capital at specified levels pursuant to applicable law and its agreement with its regulators and currently exceeds all minimum capital requirements.

In October 2017, the Federal Reserve Bank of New York terminated the formal written agreement (the "Written Agreement") entered into on June 3, 2010 between the Corporation and the Federal Reserve. However, the Corporation has agreed with its regulators to continue to obtain approval before paying dividends, receiving dividends from the Bank, making payments on subordinated debt or trust preferred securities, incurring or guaranteeing debt or purchasing or redeeming any corporate stock.

Dividend Restrictions

The Federal Reserve Board's "Applying Supervisory Guidance and Regulations on the Payment of Dividends, Stock Redemptions, and Stock Repurchases at Bank Holding Companies" (the "Supervisory Letter") discusses the ability of bank holding companies to declare dividends and to repurchase equity securities. The Supervisory Letter is generally consistent with prior Federal Reserve supervisory policies and guidance, although it 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 Board provides that the principles discussed in the letter are applicable to all bank holding companies.

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. 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).

In prior years, the principal source of funds for the Corporation's parent holding company was dividends declared and paid by its subsidiary, FirstBank. Pursuant to its agreement with the Federal Reserve, the Corporation cannot directly or indirectly take dividends or any other form of payment representing a reduction in capital from the Bank without the prior approval of the Federal Reserve. The ability of FirstBank to declare and pay dividends on its 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.

We suspended dividend payments on our common stock and preferred dividends commencing with the preferred dividend payments for the month of August 2009. We must obtain the regulators' approval before we declare, set apart or pay any dividends on any of our common stock or preferred stock. Since the fourth quarter of 2016, following receipt of the requisite regulatory approval, the Corporation has paid monthly cash dividends on its outstanding shares of Series A through E Noncumulative Perpetual Monthly Income Preferred Stock. The Corporation has to date received approval to pay the monthly dividends on the Corporation's Series A through E Preferred Stock through March 2018, although there is no assurance that such approvals for future periods will be forthcoming. Further, although there is no assurance that any dividends will be declared on the Corporation's Series A through E Preferred Stock in any future periods, the Corporation intends to continue to request the Federal Reserve's approval to enable it to continue to pay the monthly dividends on its Series A through E Preferred Stock. So long as any shares of preferred stock remain outstanding, we cannot declare, set apart or pay any dividends on shares of our common stock unless any accrued and unpaid dividends on our 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 our preferred stock for the then current month has been or is contemporaneously declared and paid or declared and set apart for payment.

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 Federal Reserve Regulation W. An affiliate of a financial institution in general 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 that 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 Dodd-Frank Act added derivatives and securities lending and borrowing transactions to the list of “covered transactions” subject to Section 23A restrictions.

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 persons, 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.

Executive Compensation

In 2010, the federal banking agencies adopted interagency guidance governing incentive-based compensation programs, which applies to all banking organizations regardless of asset size. This guidance uses a principles-based approach to ensure that incentive-based compensation arrangements appropriately tie rewards to longer-term performance and do not undermine the safety and soundness of banking organizations or create undue risks to the financial system. The interagency guidance is based on three major principles: (i) balanced risk-taking incentives; (ii) compatibility with effective controls and risk management; and (iii) strong corporate governance. The guidance further provides that, where appropriate, the banking agencies will take supervisory or enforcement action to ensure that material deficiencies that pose a threat to the safety and soundness of the organization are promptly addressed.

In May 2016, as required under section 956 of the Dodd-Frank Act, the federal banking agencies, along with other federal regulatory agencies, proposed regulations (first proposed in 2011) governing incentive-based compensation practices at covered banking institutions, which would include, among others, all banking organizations with assets of $1 billion or greater. These proposed rules are intended to better align the financial rewards for covered employees with an institution's long-term safety and soundness. Portions of these proposed rules would apply to the Corporation and FirstBank. Those applicable provisions would generally (i) prohibit types and features of incentive-based compensation arrangements that encourage inappropriate risk because they are "excessive" or "could lead to material financial loss" at the banking institution; (ii) require incentive-based compensation arrangements to adhere to three basic principles: (1) a balance between risk and reward; (2) effective risk management and controls; and (3) effective governance; and (iii) require appropriate board of directors (or committee) oversight and recordkeeping and disclosures to the banking institution's primary regulatory agency. The nature and substance of any final action to adopt these proposed rules, and the timing of any such action, are not known at this time.

Bank and Bank Holding Company Regulatory Capital Requirements

The Federal Reserve Board has adopted risk-based and leverage 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's historical risk-based capital guidelines were based upon the 1988 capital accord ("Basel I") of the Basel Committee. These historical requirements, however, which included a legacy simplified risk-weighting system for the calculations of risk-based assets, as well as lower leverage capital requirements, were superseded by new risk-based and leverage capital requirements that went into effect, on a multi-year transitional basis, on January 1, 2015. The FDIC has adopted substantively identical requirements that apply to insured banks under its regulation and supervision. These requirements are part of a revised regulatory capital framework for U.S. banking organizations (the “Basel III rules”) adopted by the banking agencies that is based on international regulatory capital requirements adopted by the Basel Committee on Banking Supervision over the past several years.

The Basel III rules introduced new minimum capital ratios and capital conservation buffer requirements, change the composition of regulatory capital, require a number of new adjustments to and deductions from regulatory capital, and introduced a new “Standardized Approach” for the calculation of risk-weighted assets that replaced the risk-weighting requirements under prior U.S. regulatory capital rules. The new minimum regulatory capital requirements and the Standardized Approach for the calculation of risk-weighted assets became effective for the Corporation on January 1, 2015. The capital conservation buffer requirements, and the regulatory capital adjustments and deductions under the Basel III rules are being phased-in over several years generally ending on December 31, 2018.

The Basel III rules introduced a new and separate ratio of Common Equity Tier 1 capital (“CET1”) to risk-weighted assets. CET1, a narrower subcomponent of total Tier 1 capital, generally consists of common stock and related surplus, retained earnings, accumulated other comprehensive income (“AOCI”), and qualifying minority interests. Certain banking organizations, however, including the Corporation and FirstBank, were allowed to make a one-time permanent election in early 2015 to continue to exclude AOCI items. The Corporation and FirstBank elected to permanently exclude capital in AOCI in order to avoid significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of the securities portfolio. In addition, the Basel III rules require the Corporation to maintain an additional CET1 capital conservation buffer of 2.5%. The capital conservation buffer must be maintained to avoid limitations on both (i) capital distributions (e.g. repurchases of capital instruments or dividend or interest payments on capital instruments) and (ii) discretionary bonus payments to executive officers and heads of major business lines. Under the fully phased-in rules, the Corporation will be required to maintain: (i) a minimum CET1 to risk-weighted assets ratio of at least 4.5%, plus the 2.5% “capital conservation buffer,” resulting in a required minimum CET1 ratio of at least 7%, (ii) a minimum ratio of total Tier 1 capital to risk-weighted assets of at least 6.0%, plus the 2.5% capital conservation buffer, resulting in a required minimum Tier 1 capital ratio of 8.5%, (iii) a minimum ratio of total Tier 1 plus Tier 2 capital to risk-weighted assets of at least 8.0%, plus the 2.5% capital conservation buffer, resulting in a required minimum total capital ratio of 10.5%, and (iv) a required minimum leverage ratio of 4%, calculated as the ratio of Tier 1 capital to average on-balance sheet (non-risk adjusted) assets. The phase-in of the capital conservation buffer began on January 1, 2016 with a first year requirement of 0.625% of additional CET1, which will be progressively increased over a four-year period, increasing by that same percentage amount on each subsequent January 1 until it reaches the fully phased-in 2.5% CET1 requirement.

In addition, the Basel III rules require a number of new deductions from and adjustments to CET1, including deductions from CET1 for certain intangible assets, and deferred tax assets dependent upon future taxable income; the four-year phase-in period for these adjustments generally began on January 1, 2015. Mortgage servicing assets and deferred tax assets attributable to temporary differences, among others, are required to be deducted to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1.

The Basel III rules also require that certain non-qualifying capital instruments, including cumulative preferred stock and trust preferred securities (“TRuPs”), be excluded from Tier 1 capital. In general, banking organizations such as the Corporation began to phase out TRuPs from Tier 1 capital on January 1, 2015. The outstanding balance owed on the

Corporation’s TRuPs were fully phased out from Tier 1 capital as of January 1, 2016. However, the Corporation’s TRuPs may continue to be included in Tier 2 capital until the instruments are redeemed or mature.

On November 21, 2017, the Federal Reserve Board, FDIC, and the Office of the Comptroller of the Currency finalized an extension of the phase-in of certain Basel III capital rules for banks not using the Basel advanced approaches. The extension, which is effective January 1, 2018, pauses the full transition to the Basel III treatment of mortgage servicing assets, certain deferred tax assets, investments in the capital of unconsolidated financial institutions and minority interests, pending the banking agencies’ broader efforts, announced in September 2017, to simply the regulatory capital rules that apply to banking organizations other than “advanced approaches” banking organizations. Because the advanced approaches rules apply only to banking organizations with more than $250 billion in total consolidated assets or at least $10 billion in total on-balance sheet foreign exposure, the extension relief applies broadly to community, midsize, and regional banks, including the Corporation and FirstBank.

The Corporation and FirstBank compute risk weighted assets using the Standardized Approach required by the Basel III rules. The Standardized Approach for risk-weightings has expanded the risk-weighting categories from the four major risk-weighting categories under the previous regulatory capital rules (0%, 20%, 50%, and 100%) to a much larger and more risk-sensitive number of categories, depending on the nature of the assets. In a number of cases, the Standardized Approach results in higher risk weights for a variety of asset categories. Specific changes to the risk-weightings of assets include, among other things: (i) applying a 150% risk weight instead of a 100% risk weight for high volatility commercial real estate acquisition, development and construction loans, (ii) assigning a 150% risk weight to exposures that are 90 days past due (other than qualifying residential mortgage exposures, which remain at an assigned risk-weighting of 100%), (iii) establishing a 20% credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable, in contrast to the 0% risk-weighting under the prior rules and (iv) requiring capital to be maintained against on-balance-sheet and off-balance-sheet exposures that result from certain cleared transactions, guarantees and credit derivatives, and collateralized transactions (such as repurchase agreement transactions).

Prompt Corrective Action. The Prompt Corrective Action ("PCA") provisions of the FDIA require the federal bank regulatory agencies to take prompt corrective action against any undercapitalized insured depository institution. The FDIA establishes five capital categories: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. Well-capitalized insured depository institutions ("institutions") significantly exceed the required minimum level for each relevant capital measure. Adequately capitalized institutions include institutions that meet but do not significantly exceed the required minimum level for each relevant capital measure. Undercapitalized institutions consist of those that fail to meet the required minimum level for one or more relevant capital measures. Significantly undercapitalized institutions are those with capital levels significantly below the minimum requirements for any relevant capital measure. Critically undercapitalized institutions have minimal capital and are at serious risk for government seizure.

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. An 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 CDs 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 CDs.

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 agencies' 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.

An 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 institution's holding company guarantees the plan up to a certain specified amount. Any such guarantee from an institution's holding company is entitled to a priority of payment in bankruptcy.

The banking agencies' Basel III rules, discussed above, revise the PCA requirements by (i) introducing a separate CET1 ratio requirement for each PCA capital category (other than critically undercapitalized) with the required CET1 ratio being 6.5% for well-capitalized status; (ii) increasing the minimum Tier 1 capital ratio requirement for each PCA capital category with the minimum Tier 1 capital ratio for well-capitalized status being 8% (as compared to the previous 6%); and (iii) eliminating the previous provision that allows a bank with a composite supervisory rating of 1 to have a 3% leverage ratio and still be adequately capitalized and maintaining the minimum leverage ratio for well-capitalized status at 5%. The Basel III rules do not change the total risk-based capital requirement (10% for well-capitalized status) for any PCA capital category. The new PCA requirements became effective on January 1, 2015.

A bank's capital category, as determined by applying the prompt corrective action provisions of the law, may not constitute an accurate representation of the overall financial condition or prospects of a bank, such as the Bank, and should be considered in conjunction with other available information regarding the financial condition and results of operations of the bank.

Set forth below are the Corporation's and FirstBank's capital ratios as of December 31, 2017 based on Federal Reserve and FDIC guidelines:

		Banking Subsidiary	
	First BanCorp.	FirstBank	General Well-Capitalized Minimum
As of December 31, 2017			
Total capital (Total capital to risk-weighted assets)	22.53%	22.06%	10.00%
Common Equity Tier 1 Capital (Common Equity Tier 1 capital to risk-weighted assets)	18.96%	17.70%	6.50%
Tier 1 capital ratio (Tier 1 capital to risk-weighted assets)	18.97%	20.79%	8.00%
Leverage ratio (1)	14.03%	15.39%	5.00%

(1) Tier 1 capital to average assets.

Deposit Insurance

The increase in deposit insurance coverage to up to $250,000 per customer, the FDIC's expanded authority to increase insurance premiums, as well as the increase in the number of bank failures after the 2008 financial crisis resulted in an increase in deposit insurance assessments for all banks, including FirstBank. The Dodd-Frank Act changed the requirements for the Deposit Insurance Fund by requiring that the designated reserve ratio for the Deposit Insurance Fund for any year not be less than 1.35 percent of estimated insured deposits or the comparable percentage of the new deposit assessment base. In addition, the FDIC must take steps as necessary for the reserve ratio to reach 1.35 percent of estimated insured deposits by September 30, 2020. If the reserve ratio exceeds 1.5 percent, the FDIC must dividend to Deposit Insurance Fund members the amount above the amount necessary to maintain the Deposit Insurance Fund at 1.5 percent, but the FDIC Board of Directors may, in its sole discretion, suspend or limit the declaration of payment of dividends. The FDIC has adopted a Deposit Reserve Fund restoration plan that projects that the designated reserve ratio will reach 1.35 percent by the 2020 deadline. The FDIC has also adopted a final rule raising its industry target ratio of reserves to insured deposits to 2 percent, 65 basis points above the statutory minimum, but the FDIC does not project that goal to be met for several years.

The FDIC assessment rules currently define the assessment base for deposit insurance as required by the Dodd-Frank Act, specify assessment rates, implement the Dodd-Frank Act's Deposit Insurance Fund dividend provisions, and revise the risk-based assessment system for all large insured depository institutions (institutions with at least $10 billion in total assets), such as FirstBank. In March 2016, the FDIC adopted a rule, which became effective on July 1, 2016, to increase the Deposit Insurance Fund to the statutorily required minimum level of 1.35 percent. Among other things, the rule imposes on banks with at least $10 billion in assets (which would include the Bank) a surcharge of 4.5 cents per $100 of their assessment base, after making certain adjustments. The FDIC has stated that it expects the reserve ratio will reach 1.35 percent before the end of 2018. If the reserve ratio does not reach 1.35 percent by the end of 2018, however, the FDIC intends to impose a shortfall assessment on March 31, 2019, on insured depository institutions with total consolidated assets of $10 billion or more.

FDIC Insolvency Authority

Under Puerto Rico banking laws (discussed below), the OCIF may appoint the FDIC as conservator or receiver of a failed or failing FDIC-insured Puerto Rican bank such as the Bank, and the FDIA authorizes the FDIC to accept such an appointment. In addition, the FDIC has broad authority under the FDIA to appoint itself as conservator or receiver of a failed or failing state bank, including a Puerto Rican bank. If the FDIC is appointed conservator or receiver of a bank upon the bank's insolvency or the occurrence of other events, the FDIC may sell or transfer some, part or all of a bank's assets and liabilities to another bank, or liquidate the bank and pay out insured depositors, as well as uninsured depositors and other creditors to the extent of the closed bank's available assets. As part of its insolvency authority, the FDIC has the authority, among other things, to take possession of and administer the receivership estate, pay out estate claims, and repudiate or disaffirm certain types of contracts to which the bank was a party if the FDIC believes such contract is burdensome and its disaffirmance will aid in the administration of the receivership. In resolving the estate of a failed bank, the FDIC as receiver will first satisfy its own administrative expenses, and the claims of holders of U.S. deposit liabilities also have priority over those of other general unsecured creditors.

Activities and Investments

The activities as "principal" of FDIC-insured, state-chartered banks such as FirstBank are generally limited to those that are permissible for national banks. Similarly, 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 eleven 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 and, as such, is required to acquire and hold shares of capital stock in the FHLB of New York in an amount 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 of New York. All loans, advances and other extensions of credit made by the FHLB to FirstBank are secured by a portion of FirstBank's mortgage loan portfolio, certain other investments and the capital stock of the FHLB held by FirstBank.

Ownership and Control

Because of FirstBank's status as an FDIC-insured bank, as defined in the Bank Holding Company Act, the Corporation, 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 adopted pursuant to the Bank Holding Company Act and the CBCA generally require prior Federal Reserve Board approval or non-objection 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 group of persons acting in concert) acquires 25% or more 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 group of persons acting in concert) acquires 10% or more of any class of voting stock and either (i) the corporation has registered securities under Section 12 of the Exchange Act, or (ii) no person (or group of persons acting in concert) 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 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 implementing regulations and guidelines of the FDIC and the other federal bank regulatory agencies 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 regulations and guidelines require, among other things, appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The regulations and guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director or principal shareholder. Failure to comply with these standards can result in administrative enforcement or other adverse actions against the bank.

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.

Puerto Rico Banking Law

As a commercial bank organized under the laws of the Commonwealth of Puerto Rico, FirstBank is subject to supervision, examination and regulation by OCIF pursuant to the Puerto Rico Banking Law of 1933, as amended (the “Banking Law”).

The Banking Law contains various provisions relating to FirstBank and its affairs, including its incorporation and organization, the rights and responsibilities of its directors, officers and stockholders and its corporate powers, lending limitations, capital requirements, and investment requirements. 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 a 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 and 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.

Section 17 of the Banking Law permits Puerto Rico commercial banks to make loans to any one person, firm, partnership or corporation in an aggregate amount of up to 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, subject to certain limitations, 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 may be wholly secured by bonds, securities and other evidences 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 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 officer, director, agent or employee 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 any such position with an affiliate 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 amount in the reserve fund equals 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, acquires 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.

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 52”)

The business and operations of FirstBank International Branch (“FirstBank IBE” or the “IBE division of FirstBank”) and FirstBank Overseas Corporation (the IBE subsidiary of FirstBank) are subject to supervision and regulation by the Commissioner. FirstBank and FirstBank Overseas Corporation were created under the IBE Act 52, which provides for total Puerto Rico tax exemption on net income derived by IBEs operating in Puerto Rico on the specific activities identified in the IBE Act. An IBE that operates as a unit of a bank pays income taxes at the corporate standard rates to the extent that the IBE’s net income exceeds 20% of the bank’s total net taxable income. Under the IBE Act 52, 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 52 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 52 and the IBE Regulations, each of FirstBank IBE and FirstBank Overseas Corporation must maintain locally books and records of all its transactions in the ordinary course of business. 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 52 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 52, 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.

In 2012, the Puerto Rico government approved Act Number 273 (“Act 273”). Act 273 replaces, prospectively, IBE Act 52 with the objective of improving the conditions for conducting international financial transactions in Puerto Rico. An IBE existing on the date of approval of Act 273, such as FirstBank IBE and FirstBank Overseas Corporation, can continue operating under IBE Act 52, or, it can voluntarily convert to an International Financial Entity (“IFE”) under Act 273 so it may broaden its scope of Eligible IFE Activities, as defined below, and obtain a grant of tax exemption under Act 273.

IFEs are licensed by the Commissioner, and authorized to conduct certain Act 273 specified financial transactions (“Eligible IFE Activities”). Once licensed, an IFE can request a grant of tax exemption (“Tax Grant”) from the Puerto Rico Department of Economic Development and Commerce, which will enumerate and secure the following tax benefits provided by Act 273 as contractual rights (i.e., regardless of future changes in Puerto Rico law) for a fifteen (15) year period:

(i) to the IFE:

- a fixed 4% Puerto Rico income tax rate on the net income derived by the IFE from its Eligible IFE Activities; and
- full property and municipal license tax exemptions on such activities.

(ii) to its shareholders:

- 6% income tax rate on distributions to Puerto Rico resident shareholders of earnings and profits derived from the Eligible IFE Activities; and
- full Puerto Rico income tax exemption on such distributions to non-Puerto Rico resident shareholders.

The primary purpose of IFEs is to attract Unites States and foreign investors to Puerto Rico. Consequently, Act 273 authorizes them to engage in traditional banking and financial transactions, principally with non-residents of Puerto Rico. Furthermore, the scope of Eligible IFE Activities encompasses a wider variety of transactions than those previously authorized to IBEs.

Act 187, as amended, enacted on November 17, 2015 requires the Commissioner to issue a Certificate of Compliance every two years in order to certify the compliance with law of companies organized under IBE Act 52.

As of the date of the issuance of this Annual Report on Form 10-K, FirstBank IBE and FirstBank Overseas Corporation are operating under IBE Act 52.

Puerto Rico Income Taxes

Under the Puerto Rico Internal Revenue Code of 2011, as amended (the “2011 PR Code”), the Corporation and its subsidiaries are treated as separate taxable entities and are not entitled to file consolidated tax returns and, thus, the Corporation is generally not entitled to utilize losses from one subsidiary to offset gains in another subsidiary. Accordingly, in order to obtain a tax benefit from a net operating loss (“NOL”), a particular subsidiary must be able to demonstrate sufficient taxable income within the applicable NOL carry-forward period. The 2011 PR Code allows entities organized as limited liability companies to perform an election to become a non-taxable “pass-through” entity and utilize losses to offset income from other “pass-through” entities, subject to certain limitations, with the remaining net income passing-through to its partner entities. The 2011 PR Code provides a dividend received deduction of 100% on dividends received from “controlled” subsidiaries subject to taxation in Puerto Rico and 85% on dividends received from other taxable domestic corporations.

Under the 2011 PR Code, First BanCorp, is subject to a maximum statutory tax rate of 39%. The 2011 PR Code also includes an alternative minimum tax of 30% 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 in Puerto Rico mainly by investing in government obligations and mortgage-backed securities exempt from U.S. and Puerto Rico income taxes and by doing business through an International Banking Entity (“IBE”) unit of the Bank, and through the Bank’s subsidiary, FirstBank Overseas Corporation, whose interest income and gain on sales is exempt from Puerto Rico income taxation. The IBE and FirstBank Overseas Corporation were created under the International Banking Entity Act of Puerto Rico, which provides for total Puerto Rico tax exemption on net income derived by IBEs operating in Puerto Rico on the specific activities identified in the IBE Act. An IBE that operates as a unit of a bank pays income taxes at the corporate standard rates to the extent that the IBE’s net income exceeds 20% of the bank’s total net taxable income.

On May 28 and September 30, 2015, the Puerto Rico legislature approved Act 72-2015 and Act 159-2015, respectively, which enacted amendments to the 2011 PR Code. The amendments related to the income tax provision include changes to the alternative minimum tax computation, and changes to the use limitation on NOLs and capital losses for 2015 and future taxable years. The change in the tax law affected the Corporation's income tax computation by limiting the NOL deduction to 80% of taxable income, compared to a 90% limitation in years prior to 2015.

Act 72-2015, as amended, also introduced a value added tax (the "VAT") on consumption, effective April 1, 2016, to replace the current sales and use tax ("SUT"), and certain temporary changes on SUT for the transition into the VAT. However, Act 54-2016, enacted on May 26, 2016, repealed the VAT sections of Act 72-2015 and made permanent the changes to SUT. The still in force changes in SUT include: an increase in tax rate from 7% to 11.5% on taxable goods and services, effective since July 1, 2015, and a 4% SUT on business to business services, and professional services, with certain exceptions, effective since October 1, 2015.

On January 24, 2018, the Government of Puerto Rico announced that it is developing a Puerto Rico Tax Reform to increase the competitiveness of the Island. The proposed plan would reduce the maximum corporate tax rate to 29% from the current 39% and would reduce business to business services sales tax to 2% from the current 4% However, such plan is subject to approval from the PROMESA oversight board and subsequent legislative action.

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 any 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 that qualify under the term "portfolio interest."

On December 22, 2017, the United States President signed H.R.1 approved by Congress (“the US Tax Reform”) including an overhaul of individual, business and international taxes, which affected our branch operations in the U.S. and the USVI. The bill includes measures reducing corporate taxes from 35% to 21%, a repeal of the corporate alternative minimum tax regime, changes to business deductions and NOLs, a 15.5% tax on mandatory repatriation of liquid assets, a 10% tax on base erosion payments and a minimum 10.5% tax on inclusion of global intangible low-tax income by U.S. shareholders, among other significant changes. The change in the tax law will also affect the Corporation’s U.S. and USVI income tax computation for 2018 by changing the limitations for FDIC premium and entertainment deductions and reducing the U.S. and USVI’s effective tax rate.

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, the licensing of employees and sales and solicitation and advertising practices, and by the Federal Reserve as to certain consumer protection provisions mandated by the GLB Act and its implementing regulations.

Mortgage Banking Operations

In addition to FDIC and CFPB regulation, FirstBank is subject to the rules and regulations of the FHA, VA, FNMA, FHLMC, GNMA, and HUD 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 audited financial statements to the FHA, VA, FNMA, FHLMC, GNMA and HUD and each regulatory entity has its own financial requirements. FirstBank’s affairs are also subject to supervision and examination by the FHA, VA, FNMA, FHLMC, GNMA and HUD at all times to assure compliance with applicable regulations, policies and procedures. Mortgage origination activities are subject to, among other requirements, the Equal Credit Opportunity Act, Federal Truth-in-Lending Act, and the Real Estate Settlement Procedures Act and the regulations promulgated thereunder that, 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 regulation by the Commissioner, with respect to, among other things, licensing requirements and the 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

RISKS RELATING TO THE CORPORATION’S BUSINESS

Uncertainty surrounding the future economic conditions that will emerge in the hurricane-impacted areas makes it difficult for management to estimate the ultimate effect of the hurricanes on credit quality, inherent loss, revenues, and asset values.

During the third quarter of 2017, two hurricanes (Maria and Irma) struck the Corporation’s service areas and caused significant damage to the infrastructure and property and severely disrupted normal economic activity in all of these regions. There is pervasive uncertainty surrounding the future economic conditions that will emerge in the hurricane-impacted areas. As a result, management is confronted with a significant and unfamiliar degree of uncertainty in estimating the impact of the recent hurricanes on credit quality, inherent loss, revenues, and asset values. In addition, there is uncertainty regarding the adequacy and timeliness of insurance recoveries, continued personal employment, the ability of businesses, including hotels, to reopen and the availability of goods and services to operate homes and businesses. Moreover, there is a significant level of uncertainty regarding the level of economic activity that will return to Puerto Rico and the Virgin Islands region over time. Some of these uncertainties include how and when rebuilding will occur, including the rebuilding of the public infrastructure, such as Puerto Rico’s power grid, how and when government, private or philanthropic funds will be invested in the affected communities, how many dislocated individuals will return to the island in both the short and long term, and what other demographic changes will take place.

During 2017, a separate qualitative element of the allowance for loan losses was determined to represent the estimate of inherent losses associated with the impact of the hurricane-related events on the Corporation’s loan portfolios. This qualitative element of the allowance was determined based on the estimated effect that the hurricanes could have on current employment levels (e.g., an unemployment rate that significantly increases from current levels in Puerto Rico based on statistics observed in the aftermath of similar natural disasters in the U.S. mainland like Hurricane Katrina), economic activity in the Corporation’s geographic regions, and the time it could take for the affected regions to return to a more normalized operating environment. For large commercial and construction loan relationships, loan officers performed individual reviews of the hurricane effect on these borrowers’ sources of repayment. However, the full extent of the adverse effect on our markets and current customers from the prolonged rebuilding efforts necessary in these areas is unknown at this time. Estimates of the hurricanes’ effect on loan losses could change over time as additional information becomes available, and any related revisions in the allowance calculation will be reflected in the provision for loan losses as they occur. Such revisions to these estimates could be material. As such, if these estimates prove to be incorrect, it may adversely impact our financial condition and results of operations.

In addition, the Corporation provided three-month deferred repayment arrangements to consumer borrowers and holders of residential mortgage loans who were affected by the hurricanes and were current in their payments or no more than 2 payments in arrears as of the date of the hurricanes. In addition, on a case by case basis, the Corporation provided three-month deferred repayment arrangements to the holders of certain commercial and constructions loans. Although early delinquency figures show improvements after the end of the deferral period in January 2018, it is currently uncertain whether all of the borrowers that have been provided with these arrangements will be able to make payments or continue to make payments on their loans given the continuing adverse economic situation in Puerto Rico. The failure of these borrowers to make such payments may adversely affect our loan portfolio and our loan servicing portfolio delinquency levels.

Lastly, the Corporation maintains force-placed insurance policies that were put into place when a borrower's insurance policy on a property was cancelled, lapsed or was deemed insufficient and the borrower did not secure a replacement policy. A borrower may make a claim against the Corporation under such force-placed insurance policy and the failure of the Corporation to resolve such a claim to the borrower's satisfaction may result in a dispute between the borrower and the Corporation, which if not adequately resolved, could have an adverse effect on the Corporation.

Our high level of non-performing loans may adversely affect our future results from operations.

We continue to have a high level of non-performing loans as of December 31, 2017, even though they decreased by $70.3 million to $497.8 million as of December 31, 2017, or 12%, from $568.2 million as of December 31, 2016. Our non-performing loans represent approximately 6% of our $8.9 billion loan portfolio as of December 31, 2017. In addition, we have a high level of total non-performing assets, even though they decreased by $83.9 million to $650.6 million as of December 31, 2017, or 11%, from $734.5 million as of December 31, 2016. The decrease in total non-performing assets was related, among other things, to the sale of the PREPA credit line with a book value of $64 million at the time of sale, and the sale of non-performing bonds of the GDB and the Puerto Rico Public Buildings Authority with an amortized cost of $23.0 million. Despite the overall decrease in non-performing assets levels for the entire year, the Corporation experienced an increase in the second half of the year, as compared to pre-hurricane levels. If we are unable to effectively maintain the quality of our loan portfolio, our financial condition and results of operations may be materially and adversely affected.

Certain funding sources may not be available to us and our funding sources may prove insufficient and/or costly to replace.

FirstBank relies primarily on customer deposits, the issuance of brokered CDs, and advances from the FHLB of New York to maintain its lending activities and to replace certain maturing liabilities. As of December 31, 2017, we had $1.2 billion in brokered CDs outstanding, representing approximately 13% of our total deposits, and a reduction of $289.2 million from the year ended December 31, 2016. Approximately $656.9 million in brokered CDs mature over the next twelve months, and the average term to maturity of the retail brokered CDs outstanding as of December 31, 2017 was approximately 1.3 years. None of these CDs are callable at the Corporation's option.

Although FirstBank has historically been able to replace maturing deposits and advances, we may not be able to replace these funds in the future if our financial condition or general market conditions change. The use of brokered deposits has been particularly important for the funding of our operations. If we are unable to issue brokered deposits, or are unable to maintain access to other funding sources, our results of operations and liquidity would be adversely affected.

Alternate sources of funding may carry higher costs than sources currently utilized. If we are required to rely more heavily on more expensive funding sources, profitability would be adversely affected. We may determine to seek debt financing in the future to achieve our long-term business objectives. Any future debt financing by the Corporation requires the prior approval of the Federal Reserve, and the Federal Reserve may not approve such financing. Additional borrowings, if sought, may not be available to us, or if available, may not be on acceptable terms. The availability of additional financing will depend on a variety of factors such as market conditions, the general availability of credit, our credit ratings and our credit capacity. In addition, the Bank may seek to sell loans as an additional source of liquidity. If additional financing sources are unavailable or are not available on acceptable terms, our profitability and future prospects could be adversely affected.

We depend on cash dividends from FirstBank to meet our cash obligations.

As a holding company, dividends from FirstBank have provided a substantial portion of our cash flow used to service the interest payments on our trust-preferred securities and other obligations. As stated above, we agreed to request approval from our regulators before receiving any cash dividends from FirstBank. In addition, FirstBank is limited by law in its ability to make dividend payments and other distributions to us based on its earnings and capital position. Our inability to receive approval from our regulators to receive dividends from FirstBank, or FirstBank's failure to generate sufficient cash flow to make dividend payments to us, may adversely affect our ability to meet all projected cash needs in the ordinary course of business and may have a detrimental impact on our financial condition.

The Banking Law of the Commonwealth of Puerto Rico requires that a minimum of 10% of FirstBank's net income for the year be transferred to a legal surplus until such surplus equals the total of paid-in-capital on common and preferred stock. Amounts transferred to the legal surplus account from the retained earnings account are not available for distribution to the stockholders without the prior consent of the Puerto Rico Commissioner of Financial Institutions. The Puerto Rico Banking Law 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 legal surplus reserve, as a reduction thereof. If there is no legal surplus reserve sufficient to cover such balance in whole or in part, the outstanding amount shall be charged against the capital account and the Bank cannot pay dividends until it can replenish the reserve fund to an amount of at least 20% of the original capital contributed. During 2017 and 2016, $7.3 million and $9.6 million, respectively, were transferred to the legal surplus reserve. FirstBank's legal surplus reserve amounted to $59.7 million and $52.4 million as of December 31, 2017 and 2016, respectively.

If we do not obtain our Regulators' approval to pay interest, principal or other sums on subordinated debentures or trust-preferred securities, a default may occur.

Following the termination of the Written Agreement, the Corporation agreed with the Federal Reserve to continue to obtain the approval of the Federal Reserve before paying dividends, receiving dividends from FirstBank, making any distributions of interest, principal or other sums on subordinated debentures or trust-preferred securities, incurring or guaranteeing debt or purchasing or redeeming any corporate stock. Although the Corporation has received regulatory approvals that has enabled it to pay scheduled quarterly interest payments on the trust-preferred securities since the second quarter of 2016, it may not receive such approvals in the future. It is the intent of the Corporation to request approvals in future periods to continue regularly scheduled quarterly interest payments on the Corporation's outstanding subordinated debentures associated with its trust-preferred securities.

Under the subordinated debentures' indentures, we have the right, from time to time, and without causing an event of default, to defer payments of interest on the subordinated debentures by extending the interest payment period at any time and from time to time during the term of the subordinated debentures for up to twenty consecutive quarterly periods. We may need to elect extension periods for future quarterly interest payments if the Federal Reserve advises us that it will not approve such future quarterly interest payments or if we do not receive the approval from our regulators before receiving any cash dividends from FirstBank given that, as mentioned above, dividends from FirstBank have provided a substantial portion of our cash flow used to service the interest payments on our outstanding subordinated debentures. Our inability to receive approval from the Federal Reserve to make distributions of interest, principal or other sums on our trust-preferred securities and subordinated debentures or to receive a cash dividend from FirstBank could result in a default under those obligations if we need to defer such payments for longer than twenty consecutive quarterly periods.

Credit quality may result in additional losses.

The quality of our loans has continued to be under pressure as a result of continued recessionary conditions in the markets we serve that have led to, among other things, high unemployment levels, low absorption rates for new residential construction projects and further declines in property values. Our business depends on the creditworthiness of our customers and counterparties and the value of the assets securing our 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, our business, financial condition, allowance levels, asset impairments, liquidity, capital and results of operations are adversely affected.

We have a commercial and construction loan portfolio held for investment in the amount of $3.8 billion as of December 31, 2017. 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. Furthermore, given the slowdown in the real estate market, the properties securing these loans may be difficult to dispose of if they are foreclosed. As of December 31, 2017, we had $294.4 million in non-performing commercial and construction loans held for investment. During 2017, the Corporation established a $68.5 million storm-related allowance for loan losses related to the estimate of inherent losses resulting from the effect of Hurricane Irma and Maria, including a $28.9 million storm-related allowance for commercial and construction loans. We may incur additional losses over the near term, either because of continued deterioration of the quality of the loans or because of sales of troubled loans, which would likely accelerate the recognition of losses. Any such losses would adversely impact our overall financial performance and results of operations.

Our allowance for loan and lease losses may not be adequate to cover actual losses, and we may be required to materially increase our allowance, which may adversely affect our capital, financial condition and results of operations.

We are subject to the risk of loss from loan defaults and foreclosures with respect to the loans we originate and purchase. We establish a provision for loan and lease losses, which leads to reductions in our income from operations, in order to maintain our allowance for inherent loan and lease losses at a level that our management deems to be appropriate based upon an assessment of the quality of the loan and lease portfolio. Management may fail to accurately estimate the level of inherent loan and lease losses or may have to increase our provision for loan and lease losses in the future as a result of new information regarding existing loans, future increases in non-performing loans, changes in economic and other conditions affecting borrowers or for other reasons beyond our control. In addition, the bank regulatory agencies periodically review the adequacy of our allowance for loan and lease losses and may require an increase in the provision for loan and lease losses or the recognition of additional classified loans and loan charge-offs, based on judgments different than those of management.

The level of the allowance reflects management's estimates based upon various assumptions and judgments as to specific credit risks, evaluation of industry concentrations, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. The determination of the appropriate level of the allowance for loan and lease losses inherently involves a high degree of subjectivity and requires management to make significant estimates and judgments regarding current credit risks and future trends, all of which may undergo material changes. If our estimates prove to be incorrect, our allowance for credit losses may not be sufficient to cover losses in our loan portfolio and our expense relating to the additional provision for credit losses could increase substantially.

Any such increases in our provision for loan and lease losses or any loan losses in excess of our provision for loan and lease losses would have an adverse effect on our future financial condition and results of operations. Given the difficulties facing some of our largest borrowers, these borrowers may fail to continue to repay their loans on a timely basis or we may not be able to assess accurately any risk of loss from the loans to these borrowers. See our risk factor "Uncertainty surrounding the future economic conditions that will emerge in the hurricane-impacted areas makes it difficult for management to estimate the ultimate effect of the hurricanes on credit quality, inherent loss, revenues and asset values" above for additional information about uncertainties surrounding the ultimate effect of the hurricanes on the affected regions.

Changes in collateral values of properties located in stagnant or distressed economies may require increased reserves.

Further deterioration of the value of real estate collateral securing our construction, commercial and residential mortgage loan portfolios would result in increased credit losses. As of December 31, 2017, approximately 1%, 18% and 37% of our loan portfolio consisted of construction, commercial mortgage and residential real estate loans, respectively.

A substantial part of our loan portfolio is located within the boundaries of the U.S. economy. Whether the collateral is located in Puerto Rico, the USVI, the BVI, or the U.S. mainland, the performance of our loan portfolio and the collateral value backing the transactions are dependent upon the performance of and conditions within each specific real estate market. Puerto Rico has been in an economic recession since 2006. Sustained weak economic conditions that have affected Puerto Rico over the last several years have resulted in declines in collateral values.

Construction and commercial loans, mostly secured by commercial and residential real estate properties, entail a higher credit risk than consumer and residential mortgage loans since they are larger in size, may have less collateral coverage, concentrate more risk in a single borrower and are generally more sensitive to economic downturns. As of December 31, 2017, commercial mortgage and construction real estate loans amounted to $1.7 billion or 20% of the total loan portfolio.

We measure the impairment of a loan based on the fair value of the collateral, if collateral dependent, which is generally obtained from appraisals. Updated appraisals are obtained when we determine 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. The appraised value of the collateral may decrease or we may not be able to recover collateral at its appraised value. A significant decline in collateral valuations for collateral dependent loans may require increases in our specific provision for loan losses and an increase in the general valuation allowance. Any such increase would have an adverse effect on our future financial condition and results of operations. During the year ended December 31, 2017, net charge-offs on construction, commercial mortgage and residential mortgage loan portfolios totaled $2.9 million, $38.8 million and $25.7 million, respectively.

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 our earnings. Net interest income is the difference between the amounts received by us on our interest-earning assets and the interest paid by us on our interest-bearing liabilities. Differences in the re-pricing structure of our assets and liabilities may result in changes in our profits when interest rates change.

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 our profits by reducing the amount of loan interest income.

Accelerated prepayments may adversely affect net interest income.

In general, fixed-income portfolio yields would decrease if the re-investment of pre-payment amounts is at lower rates. Net interest income could also be affected by prepayments of mortgage-backed securities. Acceleration in the prepayments of mortgage-backed securities would lower yields on these securities, as the amortization of premiums paid upon the acquisition of these securities would accelerate. Conversely, acceleration in the prepayments of mortgage-backed securities would increase yields on securities purchased at a discount, as the accretion of the discount would accelerate. These risks are directly linked to future period market interest rate fluctuations. Also, net interest income in future periods might be affected by our investment in callable securities because decreases in interest rates might prompt the early redemption of such securities.

Changes in interest rates on loans and borrowings may adversely affect net interest income.

Basis risk is the risk of adverse consequences resulting from unequal changes in the difference, also referred to as the “spread” or basis, between the rates for two or more different instruments with the same maturity and 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. For example, the interest expense for liability instruments such as brokered CDs might not change by the same amount as interest income received from loans or investments. To the extent that the interest rates on loans and borrowings change at different rates and by different amounts, the margin between our LIBOR-based assets and the higher cost of the brokered CDs might be compressed and adversely affect net interest income.

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

For the years ended December 31, 2015, 2016 and 2017, we recognized a total of $16.5 million, $6.7 million and $12.2 million, respectively, in other-than-temporary impairments. These impairments were primarily related to three Puerto Rico government debt securities which were sold during 2017. To the extent that any portion of the unrealized losses in our investment securities portfolio of $43.8 million as of December 31, 2017 is determined to be other-than-temporary and, in the case of debt securities, the loss is related to credit factors, we would recognize a charge to earnings in the quarter during which such determination is made and capital ratios could be adversely affected. Even if we do not determine that the unrealized losses associated with this portfolio require an impairment charge, increases in unrealized losses on available-for-sale securities adversely affect our tangible common equity ratio, which may adversely affect credit rating agency and investor sentiment towards us. Any negative perception also may adversely affect our ability to access the capital or credit markets or might increase our cost of capital. 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 our credit ratings could further increase the cost of borrowing funds.

The Corporation's ability to access new non-deposit sources of funding, even if approved by the Federal Reserve, could be adversely affected by downgrades in our credit ratings. The Corporation's liquidity is to a certain extent contingent upon its ability to obtain external sources of funding to finance its operations. The Corporation's current credit ratings and any downgrades in such credit ratings can hinder the Corporation's access to new forms of external funding and/or cause external funding to be more expensive, which could in turn adversely affect results of operations.

Defective and repurchased loans may harm our business and financial condition.

In connection with the sale and securitization of loans, we are required to make a variety of customary representations and warranties relating to the loans sold or securitized. Our obligations with respect to these representations and warranties are generally outstanding for the life of the loan, and relate to, among other things:

- compliance with laws and regulations;
- underwriting standards;
- the accuracy of information in the loan documents and loan files; and
- the characteristics and enforceability of the loan

A loan that does not comply with these representations and warranties may take longer to sell, may impact our ability to obtain third-party financing for the loan, and may not be saleable or may be saleable only at a significant discount. If such a loan is sold before we detect non-compliance, we may be obligated to repurchase the loan and bear any associated loss directly, or we may be obligated to indemnify the purchaser against any loss, either of which could reduce our cash available for operations and liquidity. Management believes that it has established controls to ensure that loans are originated in accordance with the secondary market's requirements, but mistakes may be made, or certain employees may deliberately violate our lending policies.

We are subject to certain regulatory restrictions that may adversely affect our operations.

We are subject to supervision and regulation by the Federal Reserve Board. We are a bank holding company and a financial holding company under the Bank Holding Company Act of 1956, as amended.

Financial holding companies are permitted to engage in a broader range of "financial" activities than those permitted to bank holding companies that are not financial holding companies. A financial holding company that ceases to meet certain standards is subject to a variety of restrictions, depending on the circumstances, including precluding the undertaking of new activities or the acquisition of shares or control of other companies. The Corporation currently is restricted in its ability to engage in new financial activities or the acquisition of shares or control of other companies without the prior written approval of the Board of Governors of the Federal Reserve System.

On October 3, 2017, the Federal Reserve terminated the Written Agreement entered to on June 3, 2010 between the Corporation and the Federal Reserve.

Although the Written Agreement is now terminated, the Corporation has agreed with its regulators to continue to obtain approval before paying dividends, receiving dividends from the Bank, making payments on subordinated debt or trust preferred securities, incurring or guaranteeing debt or purchasing or redeeming any corporate stock. If we fail to comply with the requirements from our regulators, we may become subject to regulatory enforcement action and other adverse regulatory actions that might have a material and adverse effect on our operations.

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

We may fail to identify and manage risks related to a variety of aspects of our business, including, but not limited to, operational risk, interest-rate risk, trading risk, fiduciary risk, legal and compliance risk, liquidity risk and credit risk. We have adopted and periodically improved various controls, procedures, policies and systems to monitor and manage risk. Any improvements to our controls, procedures, policies and systems, however, may not be adequate to identify and manage the risks in our various businesses. If our risk framework is ineffective, either because it fails to keep pace with changes in the financial markets or our businesses or for other reasons, we could incur losses or suffer reputational damage or find ourselves out of compliance with applicable regulatory mandates or expectations.

We may also be subject to disruptions from external events that are wholly or partially beyond our 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.

Failure to maintain effective internal control over financial reporting or disclosure controls and procedures could adversely affect our ability to report our financial condition and results of operations accurately and on a timely basis.

In connection with our fiscal 2017 assessment of internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act of 2002, we identified a material weakness in our internal control over financial reporting relating to the estimation procedures for the allowance for loan losses for commercial loans. For a discussion of our internal control over financial reporting and a description of the identified material weakness in our internal controls over financial reporting, see the "Management's Report on Internal Control over Financial Reporting" set forth in Item 8 of this Form 10-K.

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim consolidated financial statements will not be prevented or detected on a timely basis. As of December 31, 2017, a control deficiency existed with respect to management's review and approval of the appropriateness of certain assumptions used to estimate the allowance for loan losses for commercial loans. Specifically, management's estimate did not incorporate the actual historical loss rate for loans classified substandard in the commercial loan portfolio, that instead was determined based on a blended loss rate using aggregate historical charge-offs and portfolio balance data for loans rated as special mention, substandard, and doubtful. Although this control deficiency did not result in an adjustment to the annual financial statements as of December 31, 2017, if we are unable to remediate the identified control deficiency, our ability to record, process and report financial information accurately, and to prepare financial statements within the time periods specified by the rules and forms of the Securities and Exchange Commission, could be adversely affected. The occurrence of or failure to remediate the material weakness may adversely affect our reputation and business and the market price of our common stock and any other securities we may issue.

Cyber-attacks, system risks and data protection breaches could present significant reputational, legal and regulatory costs.

The Corporation is under continuous threat of cyber-attacks especially as we continue to expand customer services via the internet and other remote service channels. Three of the most significant cyber-attack risks that we face are e-fraud, denial-of-service and computer intrusion that might result in loss of sensitive customer data. Loss from e-fraud occurs when cybercriminals breach and extract funds from customer bank accounts. Denial-of-service disrupts services available to our customers through our on-line banking system. Computer intrusion attempts might result in the breach of sensitive customer data, such as account numbers and social security numbers, and any cyber-attacks could present significant reputational, legal and/or regulatory costs to the Corporation if successful. Our risk and exposure to these matters remains heightened because of the evolving nature and complexity of the threats from organized cybercriminals and hackers, and our plans to continue to provide electronic banking services to our customers.

If personal, non-public, confidential or proprietary information of our customers in our possession were to be mishandled or misused, we could suffer significant regulatory consequences, reputational damage and financial loss. Such mishandling or misuse could include, for example, the erroneous provision of information to parties who are not permitted to have the information, either by fault of our systems, employees, or counterparties, or the interception or other inappropriate use of such information by third parties.

We rely on other companies to perform key aspects of our business infrastructure.

Third parties perform key aspects of our business operations such as data processing, information security, recording and monitoring transactions, online banking interfaces and services, internet connections and network access. While we believe that we have selected these third-party vendors carefully, we do not control their actions. Any problems caused by these third parties, including those resulting from disruptions in communication services provided by a vendor, failure of a vendor to handle current or higher volumes, failure of a vendor to provide services for any reason, the provision by a vendor of poor performance of services, or failure of a vendor to notify us of a reportable event, could adversely affect our ability to deliver products and services to our customers and otherwise conduct our business. Financial or operational difficulties of a third-party vendor could also hurt our operations if those difficulties interfere with the vendor's ability to serve us. Replacing these third-party vendors could also create significant delay and expense. Accordingly, use of such third parties creates an inherent risk to our business operations.

Competition for our executives and other key 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 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 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 of 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 employees. Similarly, the loss of our executives or other key employees, either individually or as a group, could result in a loss of customer confidence in our ability to execute banking transactions on their behalf.

Our compensation practices are subject to review and oversight by the Federal Reserve Board. We also may be subject to limitations on compensation practices by the FDIC or other regulators, which may or may not affect our competitors. Limitations on our compensation practices could have a negative impact on our ability to attract and retain talented senior leaders in support of our long term strategy.

Our compensation practices are subject to oversight by the Federal Reserve Board and the FDIC. Any deficiencies in our compensation practices may be incorporated into our supervisory ratings, which can affect our ability to make acquisitions or perform other actions. In addition, the regulation of our compensation practices may change in the future.

Our compensation practices are subject to oversight by the Federal Reserve Board and the FDIC. As discussed above, the Corporation currently is subject to the 2010 interagency guidance governing the incentive compensation activities of regulated banks and bank holding companies. Our failure to satisfy these restrictions and guidelines could expose us to adverse regulatory criticism, lowered supervisory ratings, and restrictions on our operations and acquisition activities. In addition, the federal banking agencies have proposed new regulations under the Dodd-Frank Act that place restrictions on the incentive compensation practices of banking organizations with $1 billion or more in assets.

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

Further increases in the FDIC deposit insurance premium or in FDIC required reserves may have a significant financial impact on us.

The FDIC insures deposits at FDIC-insured depository institutions up to certain limits (currently, $250,000 per depositor account). The FDIC charges insured depository institutions premiums to maintain the Deposit Insurance Fund (the "DIF"). In the event of a bank failure, the FDIC takes control of a failed bank and, if necessary, pays all insured deposits up to the statutory deposit insurance limits 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.

The Dodd-Frank Act requires the FDIC to increase the DIF's reserves against future losses, which will require institutions with assets greater than $10 billion, such as FirstBank, to bear an increased responsibility for funding the prescribed reserve to support the DIF. Among other things, the Dodd-Frank Act requires the FDIC to bolster the DIF by increasing the required reserve ratio for the industry to 1.35 percent (the ratio of reserves to insured deposits) by September 30, 2020.

The FDIC's revised rule on deposit insurance assessments implements a provision in the Dodd-Frank Act that changes the assessment base for deposit insurance premiums from one based on domestic deposits to one based on average consolidated total assets minus average Tier 1 capital. The rule changes the assessment rate schedules for insured depository institutions so that approximately the same amount of revenue would be collected under the new assessment base as would be collected under the previous rate schedule and the schedules previously proposed by the FDIC. The rule also revises the risk-based assessment system for all large insured depository institutions (generally, institutions with at least $10 billion in total assets, such as FirstBank). Under the rule, the FDIC uses a scorecard method to calculate assessment rates for all such institutions.

In March 2016, the FDIC adopted a final rule imposing a quarterly deposit insurance assessment surcharge on banks with at least $10 billion in assets of 4.5 cents per $100 of their assessment base, after making certain adjustments once the Deposit Insurance Fund Reserve Ratio reaches or exceeds 1.15 percent. For purposes of this surcharge, the first $10 billion of assets are subtracted from the regular insurance assessment base to determine the surcharge base. The assessment surcharge became effective on July 1, 2016 and applies to FirstBank. In addition, under the Final Rule, if the Deposit Insurance Fund Reserve Ratio does not reach 1.35 percent by December 31, 2018, a shortfall assessment may be assessed on large banks in the first quarter of 2019 and collected by the FDIC on June 30, 2019. The FDIC also adopted a final rule raising its industry target ratio of reserves to insured deposits to 2 percent, 65 basis points above the statutory minimum, but the FDIC does not project that goal to be met for several years.

The FDIC may further increase FirstBank's premiums or impose additional assessments or prepayment requirements in the future. The Dodd-Frank Act has removed the statutory cap for the reserve ratio, leaving the FDIC free to set this cap going forward.

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 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, reserves we establish to cover any settlements or judgments may not be sufficient to cover our actual financial exposure, which has occurred in the past and may again occur, resulting in a material adverse 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 the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted. A securities class action suit against us could result in substantial costs, potential liabilities and the diversion of management's attention and resources.

The resolution of legal actions or regulatory matters, when unfavorable, has had and could in the future 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.

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, or our ability to attract and retain customers or obtain 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 we fail to promptly address matters that bear on our reputation, our reputation may be materially adversely affected and our business may suffer.

Changes in accounting standards issued by the Financial Accounting Standards Board may adversely affect our financial statements.

Our financial statements are subject to the application of U.S. Generally Accepted Accounting Principles ("GAAP"), which are periodically revised and expanded. Accordingly, from time to time, we are required to adopt new or revised accounting standards issued by the Financial Accounting Standards Board ("FASB"). The FASB has issued several financial accounting and reporting standards that will govern key aspects of the Corporation's financial statements or interpretations thereof when those standards become effective, including those areas where the Corporation is required to make assumptions or estimates. For example, the FASB's new accounting standard on credit losses, which will become effective for the Corporation on January 1, 2020, will require earlier recognition of credit losses on financial assets. The new accounting model requires that lifetime "expected credit losses" of financial assets not recorded at fair value through net income, such as loans and held-to-maturity securities, be recorded at inception of the financial asset, replacing the multiple existing impairment models under GAAP which generally require that a loss be "incurred" before it is recognized. For additional information on this and other accounting standards, see Note 1, *"Nature of Business and Summary of Significant Accounting Policies"* to the consolidated financial statements included in Item 8 of this Form 10-K.

Changes to financial accounting or reporting standards or interpretations, whether promulgated or required by the FASB or other regulators, could present operational challenges and could require the Corporation to change certain of the assumptions or estimates it previously used in preparing its financial statements, which could negatively impact how it records and reports its financial condition and results of operations generally and/or with respect to particular businesses. For additional information on the key areas for which assumption and estimates are used in preparing the Corporation's financial statements, see Note 1, *"Nature of Business and Summary of Significant Accounting Policies"* of the consolidated financial statements included in Item 8 of this Form 10-K.

Any impairment of our goodwill or amortizable intangible assets may adversely affect our operating results.

If our goodwill or amortizable intangible assets become impaired, we may be required to record a significant charge to earnings. Under GAAP, we review our amortizable intangible assets for impairment when events or changes in circumstances indicate that 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 us to make estimates and assumptions with regards to the fair value of our 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 our results of operations and the reporting unit where the goodwill is recorded. We conducted our most recent evaluation of goodwill during the fourth quarter of 2017.

If we are required to record a charge to earnings in our consolidated financial statements because an impairment of the goodwill or amortizable intangible assets is determined, our results of operations could be adversely affected.

Recognition of deferred tax assets is dependent upon the generation of future taxable income by the Bank.

As of December 31, 2017, the Corporation had a deferred tax asset of $294.8 million (net of a valuation allowance of $191.2 million), including $173.2 million associated with FirstBank's Net Operating Losses ("NOLs"). Under Puerto Rico law, the Corporation and its subsidiaries, including FirstBank, are treated as separate taxable entities and are not entitled to file consolidated tax returns. Accordingly, in order to obtain a tax benefit from NOLs, a particular subsidiary must be able to demonstrate sufficient taxable income. Nonetheless, the 2011 PR Code allows entities organized as limited liability companies to perform an election to become a non-taxable "pass-through" entity and utilize losses to offset income from other "pass-through" entities, subject to certain limitations, with the remaining net income passing-through to its partner entities. To obtain the full benefit of the applicable deferred tax asset attributable to NOLs, FirstBank and its pass-through entities must have sufficient taxable income within the applicable carry forward period (7 years for taxable years beginning before January 1, 2005, 12 years for taxable years beginning after December 31, 2004 and before January 1, 2013, and 10 years for taxable years beginning after December 31, 2012). The Bank incurred all of its NOLs on or after 2009. Accounting for income taxes requires that companies assess whether a valuation allowance should be recorded against their deferred tax asset based on an assessment of the amount of the deferred tax asset that is more likely than not to be realized.

The Corporation has a partial valuation allowance over its deferred tax assets in the amount of $191.2 million as of December 31, 2017. Due to significant estimates utilized in determining the valuation allowance and the potential for changes in facts and circumstances, it is reasonably possible that, in the future, the Corporation will not be able to reverse the valuation allowance or that the Corporation will need to increase its current deferred tax asset valuation allowance.

The Corporation's judgments regarding tax accounting policies and the resolution of tax disputes may impact the Corporation's earnings and cash flow.

Significant judgment is required in determining the Corporation's effective tax rate and in evaluating its tax positions. The Corporation provides for uncertain tax positions when such tax positions do not meet the recognition thresholds or measurement criteria prescribed by applicable GAAP.

Fluctuations in federal, state, local and foreign taxes or a change to uncertain tax positions, including related interest and penalties, may impact the Corporation's effective tax rate. When particular tax matters arise, a number of years may elapse before such matters are audited and finally resolved. In addition, tax positions may be challenged by the Puerto Rico Department of Treasury ("PRTD"), the United States Internal Revenue Service ("IRS") and the tax authorities in the jurisdictions in which we operate and we may estimate and provide for potential liabilities that may arise out of tax audits to the extent that uncertain tax positions fail to meet the recognition standard under applicable GAAP. Unfavorable resolution of any tax matter could increase the effective tax rate and could result in a material increase in our tax expense. Resolution of a tax issue may require the use of cash in the year of resolution.

Changes in the Tax Law in multiple jurisdictions can materially affect our operations, tax obligations and effective tax rate.

First BanCorp. is subject to Puerto Rico income tax on its income from all sources. As a Puerto Rico corporation, it is treated as a foreign corporation for U.S. and USVI income tax purposes and is generally subject to U.S. and USVI income tax only on its income from sources within the U.S. and USVI or income effectively connected with the conduct of a trade or business in those regions. The USVI jurisdiction imposes income taxes based on the U.S. Internal Revenue Code under the "mirror system" established by the Naval Service Appropriations Act of 1922. However, the USVI jurisdiction also imposes an additional 10% surtax on the USVI tax liability, if any.

These tax laws are complex and subject to different interpretations. We must make judgments and interpretations about the application of these inherently complex tax laws when determining our provision for income taxes, our deferred tax assets and liabilities, and our valuation allowance. In addition, legislative changes, particularly changes in tax laws, could adversely impact our results of operations.

On December 22, 2017, the United States president signed H.R.1, approved by Congress, including an overhaul of individual, business and international taxes, which impacts corporations doing business in the U.S. and the USVI. The

US Tax Reform requires new computations to be performed that were not previously required in U.S. tax law and judgment is required in the interpretation of the provisions of the US Tax Reform. Some international provisions of the US Tax Reform, such as the GILTI tax, could also result in the relocation of U.S. Controlled Foreign Corporations ("CFC") doing business in Puerto Rico which could have a significant impact on the economy of Puerto Rico and consequently on the operations of the Corporation. Also, the US Tax Reform could trigger changes in tax law or increase taxes in the USVI jurisdiction in order to offset the effects of the reduction in income tax rate in the USVI.

On January 24, 2018 the Government of Puerto Rico announced that it is developing a Puerto Rico Tax Reform, which would reduce corporate tax rates, to increase competitiveness of the Island after the enactment of the US Tax Reform. However, such plan is subject to approval from the PROMESA oversight board and subsequent legislative action.

Changes in Puerto Rico, U.S. or other jurisdiction's applicable tax laws or tax authorities' new interpretations, could result in increases in our overall taxes and the Corporation's financial condition or results of operations may be adversely impacted.

Our ability to use our net operating loss (NOL) carryforwards may be limited.

The Corporation has Puerto Rico, U.S. and USVI sourced NOL's carryforwards. Section 382 of the U.S. Internal Revenue Code ("Section 382") and Section 1034.04(u) of the Puerto Rico Internal revenue Code ("Section 1034.04(u)"), which is significantly similar to Section 382, limit the ability to utilize U.S., USVI and Puerto Rico NOLs, respectively, at such jurisdictions following an event of an ownership change. Generally, an ownership change occurs when certain shareholders increase their aggregate ownership by more than 50 percentage points over their lowest ownership percentage over a three-year testing period. However, Puerto Rico Section 1034.04(u) has a particular exemption ("the Capital Raise Exemption"), which allows a change in control to be exempt from Section 1034.04(u) if the purpose of the issuance is to raise capital for the operations of the entity, and immediately after the issuance, and for no less than five years, the entity's shares are marketed in one or more recognized stock exchanges. Upon the occurrence of a Section 382 or Section 1034.04(u) ownership change, the use of NOLs attributable to the period prior to the ownership change is subject to limitations and only a portion of the U.S., USVI and Puerto Rico NOLs, as applicable, may be used by the Corporation to offset the annual U.S., USVI and Puerto Rico taxable income, if any. During 2017, the Corporation completed a formal ownership change analysis within the meaning of Section 382 covering a comprehensive period, and concluded that an ownership change, for U.S. and USVI purposes only, occurred during the period evaluated. The Section 382 limitation resulted in higher U.S. liabilities than we would have incurred in the absence of such limitation.

Furthermore, it is possible that the utilization of our Puerto Rico, U.S. and USVI NOLs could be further limited due to future changes in our stock ownership, as a result of either sales of our outstanding shares or issuances of new shares that could separately or cumulatively trigger an ownership change and, consequently, a Section 1034.04(u) or Section 382 limitation. Any Section 1034.04(u) limitation for Puerto Rico could result in material adjustments to our deferred tax assets, earnings and cash flows. Any further Section 382 limitations may result in greater U.S. and USVI tax liabilities than we would incur in the absence of such a limitation and any increased liabilities could adversely affect our earnings and cash flow. We may be able to mitigate the adverse effects associated with a Section 382 limitation in the U.S. and USVI to the extent that we could credit any resulting additional U.S. and USVI tax liability against our tax liability in Puerto Rico. However, our ability to credit U.S. and USVI taxes against Puerto Rico taxes is subject to limitations and will depend on our tax profile and other factors at each annual taxable period.

We must respond to rapid technological changes, and these changes may be more difficult or expensive than anticipated.

If competitors introduce new products and services embodying new technologies, or if new industry standards and practices emerge, our existing product and service offerings, technology and systems may become obsolete. Further, if we fail to adopt or develop new technologies or to adapt our products and services to emerging industry standards, we may lose current and future customers, which could have a material adverse effect on our business, financial condition and results of operations. The financial services industry is changing rapidly and, in order to remain competitive, we must continue to enhance and improve the functionality and features of our products, services and technologies. These changes may be more difficult or expensive than we anticipate.

RISKS RELATING TO THE BUSINESS ENVIRONMENT AND OUR INDUSTRY

Continuation of the economic slowdown and decline in the real estate market in Puerto Rico could continue to harm our 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 has declined over the past few years and this trend may continue to reduce the level of mortgage loans we produce in the future and adversely affect our business. During periods of rising interest rates, the refinancing of many mortgage products tends 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.

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

The Corporation's credit quality and the value of our portfolio of Puerto Rico government securities has been and in the future may be adversely affected by Puerto Rico's economic condition, and may be affected by actions taken by the Puerto Rico government or the PROMESA oversight board to address the ongoing fiscal and economic challenges in Puerto Rico.

A significant portion of our financial activities and credit exposure is concentrated in the Commonwealth of Puerto Rico, which has been in an economic recession since 2006, exacerbated by the effect of Hurricanes Irma and Maria in 2017. Based on the most recent information available included in the Revised Fiscal Plan submitted by the Puerto Rico government for the review of the PROMESA oversight board, Puerto Rico's GNP has shrunk by more than 14% since 2006. For fiscal year 2018, the Puerto Rico government projects a contraction in the Puerto Rico's GNP of 11.0%, followed by projected growths of 8.4% and 3.5% for fiscal years 2019 and 2020, respectively, based on an assumption of Puerto Rico's receipt of $49.1 billion of Federal Disaster Relief assistance and $21 billion from private insurance funds. Meanwhile, the GDB-EAI in December 2017 was 104.9, a 14.0% reduction compared to December 2016, and a decrease of 13.3% compared to August 2017. The GDB-EAI is a coincident index of economic activity for Puerto Rico made up of four indicators (non-farm payroll employment, electric power generation, cement sales and gasoline consumption). The Revised Fiscal Plan states that the hurricanes will create a spike in inflation of 2.1% in fiscal year 2018, with subsequent average increases of about 1.5% over the next six years, until fiscal year 2023.

The seasonally adjusted unemployment rate in Puerto Rico was 10.9% in December 2017, compared to 12.4% in December 2016. However, the Puerto Rico labor force participation rate was 40.9% as of December 2017. The average of the labor force participation rate in Puerto Rico was 45.05% from 1990 until 2017, reaching an all-time high of 49.80% percent in February of 2007 and a record low of 38.6% in October of 2017. Based on information published by the Puerto Rico government, the labor force estimate was 1.1 million people for December 2017, a reduction of 1.6% when compared with December 2016. The Revised Fiscal Plan reflects that a 20% cumulative decline in population is expected over the next six years.

Based on information published by the Puerto Rico Treasury, the net revenues of the Puerto Rico government's General Fund in December 2017 totaled $697.6 million, which was $101.9 million less than in December 2016. The net revenues to the General Fund for the first half of fiscal year ending June 30, 2018 totaled $3,623.1 million, a decrease of $348.0 million, or 8.8%, compared with the previous fiscal year, and, $157.3 million, or 4.3%, below initial estimates for this period. The Revised Fiscal Plan reflects a projected decline in revenues of 19.8% in fiscal year 2018 before increasing 10.2% in fiscal year 2019 and 5.1% in fiscal year 2020. As per the Revised Fiscal Plan, revenues are forecasted to become 3% higher than pre-hurricane levels by fiscal year 2023, in nominal terms.

Prices on most Commonwealth of Puerto Rico securities have decreased over the past months. General obligations with an eight percent coupon and maturing in 2035 traded in January at an average of 25 cents on the dollar, down from as much as 59 cents in September, before the hurricane.

On May 3, 2017, the Puerto Rico government and the PROMESA oversight board filed for a form of bankruptcy in the U.S. District court in Puerto Rico under Title III of PROMESA. The Title III provision allows for a court debt restructuring process similar to U.S. bankruptcy protection. On July 2, 2017, the PROMESA oversight board filed for a similar Title III form of bankruptcy in the U.S. District court in Puerto Rico for PREPA.

During the third quarter of 2017, Hurricanes Irma and Maria affected Puerto Rico causing significant damage to the infrastructure and property. In the aftermath of Hurricane Maria, the NOAA stated that damages could totalize $90 billion. The emergency could cause Puerto Rico's central government and some of its instrumentalities to face severe cash shortfalls from lower revenues, higher cost, and delayed or reduced cost-saving measures that had been required by the fiscal plans previously approved early in 2017.

The Puerto Rico government and the PROMESA oversight board requested federal assistance from the United States government. Such assistance is intended to provide Puerto Rico with the cash that it will need to operate its core government services and its disaster response effort in the near future. On December 18, 2017, the U.S. House of Representative introduced a bill to provide additional emergency assistance for the recent hurricanes, wildfires in California, and related agriculture losses. The bill totals $81 billion and targets funds to programs to continue relief and recovery efforts in all of the affected communities, including Texas, Florida, California, Louisiana, Puerto Rico and the USVI.

On February 9, 2018, the Puerto Rico Governor and the Resident Commissioner announced an allocation of $16 billion in federal funds for the island's recovery after Hurricane Maria. This appropriation is part of budget legislation approved by the U.S. Congress and signed by the President of the United States on February 9, 2018. Approximately $11.0 billion of the $16.0 billion was allocated to the community development fund, known as the Community Development Block Grant, to repair homes, support local businesses and rebuild infrastructure while mitigating future risks. From this figure, $2.0 billion will be designated to restore and make improvements to the electrical system. In addition, $1.37 billion was approved for emergency assistance and $150 million under the Direct Loan Program to cover cost sharing with FEMA. In addition to the $16.0 billion, Puerto Rico is also eligible to participate in other programs that could increase aid to the island to more than $45 billion.

On February 12, 2018, the FAFAA released the Revised Fiscal Plan for the Commonwealth, after considering the changes and clarifications required by the PROMESA oversight board to a previous draft. The Fiscal Plan includes substantial revisions that the Puerto Rico government has made to the previous fiscal plan, certified on March 13, 2017, to account for the effect of Hurricanes Maria and Irma and to account for a contemplated transformational transaction. The Revised Fiscal Plan uses a six-year horizon, projects a six-year cumulative decline in population of 20%, and projects that by the fiscal year 2023 there will be a $3.4 billion surplus, before any debt service is paid, requiring a liquidity facility to provide public services in fiscal year 2018. The March 2017 fiscal plan covered a 10-year period and allocated around $787 million per year for debt service. The Revised Fiscal Plan also includes projected expenses for Title III proceedings, considers an injection of $49 billion in federal relief assistance, and a series of structural reforms in, among others things, the areas of ease of doing business, human capital, tax reform, and power sector reform, including a layout for the privatization of PREPA. The Revised Fiscal Plan also creates an annual reserve of $130 million and a $400 million investment for infrastructure maintenance and development. The PROMESA oversight board is expected to evaluate the plan in the coming weeks and, after a public hearing, determine whether to certify it.

As of December 31, 2017, the Corporation had $214.5 million of direct exposure to the Puerto Rico government, its municipalities and public corporations, compared to $323.3 million as of December 31, 2016. As of December 31, 2017, approximately $184.6 million of the exposure consisted of loans and obligations of municipalities in Puerto Rico that are supported by assigned property tax revenues and for which, in most cases, the good faith, credit and unlimited taxing power of the applicable municipality have been pledged to their repayment. These municipalities are required by law to levy special property taxes in such amounts as are required for the payment of all of their respective general obligation bonds and loans. The PROMESA oversight board has not designated any of Puerto Rico's 78 municipalities as covered entities under PROMESA. However, while the Revised Fiscal Plan did not contemplate a restructuring of the debt of Puerto Rico's municipalities, the plan did call for the gradual elimination of budgetary subsidies provided to municipalities by the central government. Furthermore, municipalities are also likely to be affected by the negative economic and other effects resulting from expense, revenue or cash management measures taken to address the Puerto Rico Government's budgetary and liquidity shortfalls, or measures included in fiscal plans of other government entities, such as the GDB Restructuring Support Agreement. In addition to municipalities, the total direct exposure also includes a $6.8 million loan to a unit of the central government and a $15.1 million loan to an affiliate of a public corporation. The Corporation's total direct exposure also includes obligations of the Puerto Rico Government, specifically bonds of the Puerto Rico Housing Finance Authority, at an amortized cost of $8.0 million as part of its available-for-sale investment securities portfolio recorded on its books at a fair value of $6.8 million as of December 31, 2017.

Furthermore, as of December 31, 2017, the Corporation had three commercial mortgage loans granted to the hotel industry in Puerto Rico that were previously guaranteed by the TDF with an outstanding principal balance of $120.2 million (book value of $70.8 million), compared to $127.7 million outstanding (book value of $111.8 million) as of December 31, 2016. Historically, the borrower and the operations of the underlying collateral of these loans have been the primary sources of repayment and the TDF, which is a subsidiary of the GDB, provided a secondary guarantee for payment performance. As part of agreements executed in the second quarter of 2017 and first quarter of 2018, the TDF paid $7.6 million and $4.0 million, respectively, to honor a portion of its guarantee on these loans.   As provided in the agreements, the cash payments received by the Corporation released the TDF from its liability as a guarantor of these loans. As a result, the income-producing real estate properties are now the only collateral of such loans, thus, any decline in collateral valuations may require additional impairments on these loans. All the three TDF commercial mortgage loans have been classified as non-performing and impaired since the first quarter of 2016, and interest payments have been applied against principal since then. Approximately $4.7 million of interest payments received on loans guaranteed by the TDF since late March 2016 have been applied against principal. During 2017, the Corporation recorded charge-offs totaling $30.8 million on these facilities for the portion of the recorded investment in excess of the fair value of the collateral and the guarantee, considering the aforementioned agreements reached with the TDF. In addition, GDB agreed to issue to the Bank a fixed income financial instrument pursuant to the GDB's Restructuring Support Agreement approved by the PROMESA oversight board. As of December 31, 2017, the non-performing TDF commercial mortgage loans and related facilities are being carried (net of reserves and accumulated charge-offs) at 52% of the unpaid principal balance.

In addition, the Corporation had $116.5 million in exposure to residential mortgage loans that are guaranteed by the PRHFA. Residential mortgage loans guaranteed by the PRHFA are secured by the underlying properties and the guarantees serve to cover shortfalls in collateral in the event of a borrower default. The Puerto Rico government guarantees up to $75 million of the principal guaranteed under the mortgage loan insurance program. According to the most recently released audited financial statements of the Puerto Rico Housing Financing Authority, as of June 30, 2015, the PRHFA's mortgage loan insurance program covered loans in an aggregate of approximately $552 million. The regulations adopted by the PRHFA require the establishment of adequate reserves to guarantee the solvency of the mortgage loan insurance fund. As of June 30, 2015, the most recent date as to which information is available, the PRHFA had a restricted net position for such purposes of approximately $77.4 million.

As of December 31, 2017, the Corporation had $490.3 million of public sector deposits in Puerto Rico, compared to $408.8 million as of December 31, 2016. As of December 31, 2017, approximately 29% of the public sector deposits in Puerto Rico are from municipalities and municipal agencies and 71% are from public corporations and the central government and agencies.

The decline in Puerto Rico's economy since 2006 and the effects of Hurricanes Irma and Maria in 2017 have resulted in, among other things, a decline in our loan originations, an increase in the level of our non-performing assets and higher loan loss provisions and charge-offs, all of which adversely affected our profitability. Any further deterioration of economic activity could result in further adverse effects on our profitability and credit quality.

***Puerto Rico Government's filing for bankruptcy may adversely impact our financial condition or results of operations*.**

On May 3, 2017, the Puerto Rico government and the PROMESA oversight board filed for a form of bankruptcy in the U.S. District Court in Puerto Rico under Title III of PROMESA. The Title III provision allows for a court debt restructuring process similar to U.S. bankruptcy protection. Since this is the first time that any state or territory of the United States has ever filed for relief that is expected to be comparable to bankruptcy relief because of the absence, until PROMESA, of any legal authority for such a relief, it is uncertain what impact this filing will have on the Corporation. A similar Title III form of bankruptcy was filed for PREPA on July 2, 2017. The Corporation's financial condition and results of operations may be negatively affected as a result of the resolution of the bankruptcy relief filing and further adverse developments in the Puerto Rico government's fiscal situation given the Corporation's direct exposure to the Puerto Rico government (excluding municipalities) of $8.0 million of Puerto Rico government debt securities, a $6.8 million loan to an agency of the Puerto Rico central government, and a $15.1 million loan to a PREPA affiliate.

Continuation of the economic slowdown and decline in the U.S. Virgin Islands could continue to harm our results of operations.

The fiscal health of the government of the USVI over the past 10 years has shown signs of deterioration evidenced by persistent budgetary deficits and projected future revenue shortfalls. The government of the USVI developed a five-year financial plan, designed to return the general fund to fiscal stability. The fiscal stabilization plan included a number of revenue enhancement initiatives as well as reductions to government operating expenses. Many of the USVI government's revenue enhancement initiatives are subject to legislative approval and are in the form of tax increases that could potentially have an adverse effect on the economy. The fiscal stabilization plan is also predicated on access of the government to the financial markets in order to issue deficit financing to cover the operating deficits from 2017 and 2018.

The passage of hurricanes Irma and Maria through the region caused significant damage to its core infrastructure, including housing, electricity and the government's ability to provide certain essential services. Since the hurricane, most schools have reopened, over 96% of energy and water consumers have service, street light fixtures have been repaired or replaced, and tourism has been slowly recovering. Considering the aforementioned challenges, the government has decided to amend the Five Year Strategic Plans in order to create new revenues, reduce public spending, and to create a fair salary payment to public employees. Further declines in the economic activity of this region could result in further adverse effects on our profitability and credit quality.

As of December 31, 2017, the Corporation has total exposure to the USVI government and its instrumentalities of $70.4 million, approximately $47.2 million was owed by public corporations of the USVI and $23.2 million was owed by an independent instrumentality of the USVI government. All loans are currently performing and up to date on principal and interest payments.

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

Given that most 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, we are exposed to downturns in the U.S. economy, including factors such as unemployment and underemployment levels in the United States and real estate valuations. The deterioration of these conditions could adversely affect the credit performance of mortgage loans, credit default swaps and other derivatives, and result in significant write-downs of asset values by financial institutions, including government-sponsored entities as well as major commercial banks and investment banks.

Despite improving labor markets in the U.S. in the past year, an elevated amount of underemployment and household debt, the volatile interest rate environment, along with a continued sluggish recovery in the consumer real estate market and certain commercial real estate markets in the U.S. pose challenges for the U.S. economic performance and the financial services industry.

In particular, we may face the following risks:

- Our 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.

- Our 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 and repurchase agreements) on favorable terms, or at all, could be adversely affected by further disruptions in the capital or credit 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.

- We expect to face increased regulation of our industry. Compliance with such regulation may increase our costs and limit our ability to pursue business opportunities.

- There may be downward pressure on our stock price.

The deterioration of economic conditions in the U.S. and disruptions in the financial markets could adversely affect our ability to access capital, our business, financial condition and results of operations.

The failure of other financial institutions could adversely affect us.

Our ability to engage in routine funding transactions could be adversely affected by future failures of financial institutions and the actions and commercial soundness of other financial institutions. Financial institutions are interrelated as a result of trading, clearing, counterparty and other relationships. We have 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, we are 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, we may experience delays in recovering the assets posted as collateral, or we may incur a loss to the extent that the counterparty was holding collateral in excess of the obligation to such counterparty.

In addition, many of these transactions expose us 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 us cannot be realized or is liquidated at prices not sufficient to recover the full amount of the loan or derivative exposure due to us. Any losses resulting from our routine funding transactions may materially and adversely affect our financial condition and results of operations.

Legislative and regulatory actions taken now or in the future may increase our costs and impact our business, governance structure, financial condition or results of operations.

We and our subsidiaries 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.

The financial crisis of 2008 resulted in regulatory agencies and political bodies placing increased focus and scrutiny on the financial services industry. The U.S. government intervened on an unprecedented scale, responding 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 to additional restrictions, oversight and costs. In addition, new proposals for legislation are periodically 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 the industry to conduct business consistent with historical practices, including in the areas of 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.

Regulatory uncertainty caused by financial deregulation measures proposed by the Trump administration and members of the U.S. Congress may increase competition in certain of our investment strategies and adversely affect our business, financial condition and results of operations.

The Trump administration's short-term legislative agenda includes certain deregulatory measures for the U.S. financial services industry, including changes to the Volcker Rule, the U.S. Risk Retention Rules, the Basel III capital requirements, the U.S. Treasury's Financial Stability Oversight Council's (the "FSOC's") authority and other aspects of the Dodd-Frank Act. On February 3, 2017, President Trump signed an executive order calling for the administration to review U.S. financial laws and regulations in order to determine their consistency with a set of core principles identified in the order. One bill, the Financial CHOICE Act (the "CHOICE Act"), which has been passed by the U.S. House of Representatives but has not been enacted into law as of this date, is being discussed as an avenue for amending Dodd-Frank. The current version of the CHOICE Act would eliminate the power of the FSOC to designate non-bank financial institutions as systematically important, repeal the Volcker Rule and change the structure and powers of the Consumer Financial Protection Bureau. In addition, the CHOICE Act would allow certain qualifying banking organizations with a satisfactory composite supervisory rating and a non-risk weighted leverage ratio of at least 10% to elect to be exempt from enhanced risk-weighted capital ratios, liquidity requirements and other regulations currently applicable to large banking organizations. It would also revise the U.S. Risk Retention Rules to remove the risk retention requirement for all asset-backed securitizations other than for certain non-qualifying residential mortgage securitizations. The CHOICE Act also would significantly alter stress testing, possibly exempting qualifying banking organizations from stress testing altogether and eliminating the Federal Reserve Board's ability to make "qualitative" objections to capital plans submitted by other banking organizations. In addition, the CHOICE Act would also significantly enhance the SEC's enforcement capabilities and increase the maximum civil penalties and criminal sanctions under federal securities laws, including under the Investment Company Act of 1940 and the Investment Advisers Act of 1940. The U.S. Senate similarly is considering more limited changes to the Dodd-Frank Act, including measures to lessen the regulatory burdens on community and mid-sized banking organizations.

Whether the CHOICE Act or the U.S. Senate bill will be enacted, and, if so, whether additional amendments would be added during the legislative process remains unclear. In the absence of legislative change, however, the Trump administration may influence the substance of regulatory supervision through, among other things, the appointment of individuals to the Federal Reserve Board, the FDIC and the CFPB. The administration recently nominated, and the Senate confirmed, Jerome Powell as Chair of the Federal Reserve Board, and Randal Quarles as a Governor and new Vice Chairman for Supervision. Further, President Trump is expected to nominate persons to fill several other of the Federal Reserve Board's seven seats. In turn, the appointment of new Federal Reserve Board members may increase the likelihood that the Federal Reserve Board modify the capital and liquidity requirements for U.S. banking organizations that are more stringent than those that have been agreed upon at the international level, including the Basel Committee on Banking Supervision's Basel III framework. The Trump administration has also nominated Jelena McWilliams, a former Senate Banking Committee senior staff member and banking industry executive, as Chair of the FDIC.

The CFPB's programs and operations may be affected by the designation of Mick Mulvaney, director of the Office of Management and Budget, as acting Director of the CFPB, and by President Trump's likely nomination in the future of a permanent Director. Mr. Mulvaney's initial actions as acting Director have been largely consistent with the announced deregulatory agenda of the Trump administration. The impact of these and other future actions on the CFPB's regulatory and enforcement activities as they affect FirstBank, however, cannot be predicted with any certainty at this time.

Measures focused on deregulation of the U.S. financial services industry may have the effect of increasing competition for our credit-focused businesses or otherwise reducing investment opportunities. Increased competition from banks and other financial institutions in the credit markets could have the effect of reducing credit spreads, which may adversely affect the revenues of our credit and other businesses whose strategies include the provision of credit to borrowers.

Determining the full extent of the impact on us of any such potential financial reform legislation, or whether any such particular proposal will become law, or the impact of regulatory changes in the absence of legislation at this point in time is highly speculative. However, any such changes may impose additional costs on us, require the attention of our senior management or Board or result in limitations on the manner in which business is conducted.

Financial services legislation and regulatory reforms may have a significant impact on our business and results of operations and on our credit ratings.

As discussed above, the Dodd-Frank Act significantly changed the regulation of financial institutions and the financial services industry. The Dodd-Frank Act includes, and the regulations developed and to be developed thereunder include or will include, provisions affecting large and small financial institutions alike. In addition, U.S. banking organizations, including the Corporation and FirstBank, are subject to new and more stringent regulatory capital requirements that generally increase the amounts of capital that we need to hold.

As of December 31, 2017, the Corporation had $202 million in trust-preferred securities that are now subject to the full phase-out from Tier 1 capital under the final regulatory capital rules discussed above.

Although First BanCorp. and FirstBank were able to meet general well-capitalized capital ratios upon implementation of the requirements, and we expect both companies will continue to exceed the minimum risk-based and leverage capital ratio requirements for well-capitalized status under the new capital rules, we may not remain at such levels.

Additional regulatory proposals and legislation, if finally adopted, could change banking laws and our operating environment and that of our subsidiaries in substantial and unpredictable ways. The ultimate effect that such legislation, if enacted, or regulations would have upon our financial condition or results of operations may be adverse.

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

Under regulatory capital adequacy guidelines, and other regulatory requirements, the Corporation and our banking subsidiary 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 certain capital levels, or are deemed not well managed under regulatory exam procedures, or if we experience certain regulatory violations, our status as a financial holding company, and our ability to offer certain financial products will be compromised and our financial condition and results of operations could be adversely affected.

Rulemaking changes implemented by the CFPB will result in higher regulatory and compliance costs related to originating and servicing residential mortgage loans and may adversely affect our results of operations.

The Dodd-Frank Act significantly changed the regulation of single-family residential mortgage lending in the United States. Among other things, the law transferred rule-making and enforcement powers from a number of federal agencies to the CFPB, imposed new risk retention and recordkeeping requirements on lenders (such as the Bank) that sell single-family residential mortgage loans in the secondary market, required revision of disclosure documents, limited loan originator compensation and expanded recordkeeping and reporting requirements under other federal statutes.

New regulations implement the Dodd-Frank Act amendments to the Equal Credit Opportunity Act, the Truth in Lending Act, and the Real Estate Settlement Procedures Act. See “Business – Regulation and Supervision – Consumer Financial Protection Bureau.”

Among other consequences of these numerous changes, the requirements relating to the evaluation of the borrower’s ability to repay the loan may result in reduced credit availability and higher borrowing costs to cover the costs of compliance. The ability of borrowers to raise new defenses in foreclosure proceedings on defaulted mortgage loans also may lead to increased foreclosure costs, extend foreclosure timelines, and increase the severity of loan losses. Increased repurchase and indemnity requests with respect to mortgage loans sold into the secondary markets may also result.

These and other changes required by the Dodd-Frank Act have required substantial modifications to the entire mortgage lending and servicing industry. Their impact may involve changes to our operations and increased compliance costs in making single-family residential mortgage loans.

Compliance with stress testing requirements may be challenging.

The Corporation is currently subject to supervisory guidance for stress testing practices issued by the federal banking agencies. The current guidance outlines broad principles for a satisfactory stress testing framework and describes various stress testing approaches and how stress testing should be used at various levels within an organization. As previously discussed, the Corporation is also subject to two new stress testing rules that implement provisions of the Dodd-Frank Act, one issued by the Federal Reserve Board that applies to First BanCorp. on a consolidated basis and one issued by the FDIC that applies to the Bank.

The Corporation submitted its third annual company-run stress test to regulators in July 2017, which was published in October 2017.

Future public disclosure of stress test results could result in reputational harm if the Corporation's results are worse than those of its competitors or otherwise indicate that the Corporation's risk profile is excessive or elevated. Furthermore, given that the Corporation will be subject to multiple stress testing requirements that are administered at different levels by more than one federal banking agency, and compliance with such requirements will be complicated, if the Corporation fails to fully comply with these requirements, it may be subject to regulatory action.

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

In addition to being affected by general economic conditions, our earnings and growth are affected by the policies of the Federal Reserve Board. An important function of the Federal Reserve Board is to regulate the money supply and credit conditions. 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 for 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 business, financial condition and results of operations may be adverse.

We are subject to numerous laws designed to protect consumers, including the Community Reinvestment Act and fair lending laws, and failure to comply with these laws could lead to a wide variety of sanctions.

The Community Reinvestment Act, the Equal Credit Opportunity Act, the Fair Housing Act and other fair lending laws and regulations impose nondiscriminatory lending requirements on financial institutions. The U.S. Department of Justice and other federal agencies are responsible for enforcing these laws and regulations. A successful regulatory challenge to an institution's performance under the Community Reinvestment Act or fair lending laws and regulations could result in a wide variety of sanctions, including damages and civil money penalties, injunctive relief, restrictions on mergers and acquisitions activity, restrictions on expansion and restrictions on entering new business lines. Private parties may also have the ability to challenge an institution's performance under fair lending laws in private class action litigation. Such actions could have a material adverse effect on our business, financial condition and results of operations.

We face a risk of noncompliance and enforcement action related to the Bank Secrecy Act and other anti-money laundering statutes and regulations.

The Bank Secrecy Act, the USA PATRIOT Act, and other laws and regulations require financial institutions, among other duties, to institute and maintain an effective anti-money laundering program and file suspicious activity and currency transaction reports as appropriate. The Financial Crimes Enforcement Network is authorized to impose significant civil money penalties for violations of those requirements and has recently engaged in coordinated enforcement efforts with the individual federal banking regulators, as well as the U.S. Department of Justice’s Drug Enforcement Administration. We are also subject to increased scrutiny of compliance with trade and economic sanctions requirements and rules enforced by OFAC. If our policies, procedures and systems are deemed deficient, we would be subject to liability, including fines and regulatory actions, which may include restrictions on our ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of our business plan, including our acquisition plans. Failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us. Any of these results could have a material adverse effect on our business, financial condition and results of operations.

RISKS RELATING TO AN INVESTMENT IN THE CORPORATION’S COMMON AND PREFERRED STOCK

Issuance of additional equity securities in the public markets and other capital management or business strategies that we may pursue could depress the market price of our common stock and could result in dilution of holders of

our common stock, including purchasers of our common stock under the resale registration statement.

Generally, we are not restricted from issuing additional equity securities, including common stock. We may choose to sell additional equity securities, or we could be required in the future to identify, consider and pursue additional capital management strategies to bolster our capital position. We may issue equity securities (including convertible securities, preferred securities, and options and warrants on our common or preferred stock securities) in the future for a number of reasons, including to finance our operations and business strategy, adjust our leverage ratio, address regulatory capital concerns, restructure currently outstanding debt or equity securities or satisfy our obligations upon the exercise of outstanding options or warrants. Future issuances of our equity securities, including common stock, in any transaction that we may pursue may dilute the interests of our existing holders of our common stock and preferred stock and cause the market price of our common stock to decline.

The Corporation has outstanding a warrant held by the U.S. Treasury to purchase 1,285,899 shares of common stock. If the warrant is exercised, the issuance of shares of common stock could reduce our income per share, and further reduce the book value per share and voting power of our current common stockholders.

The market price of our common stock may continue to be subject to significant fluctuations and volatility.

The stock markets have frequently experienced high levels of volatility since 2008. These market fluctuations have adversely affected, and may continue to adversely affect, the trading price of our common stock. In addition, the market price of our common stock has been subject to significant fluctuations and volatility because of factors specifically related to our businesses and may continue to fluctuate or decline.

Factors that could cause fluctuations, volatility or a decline in the market price of our common stock, many of which could be beyond our control, include the following:

- uncertainties and developments related to the resolution of the Puerto Rico government's fiscal problems;

- any regulatory actions against us;

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

- announcements of strategic developments, acquisitions and other material events by us or our competitors, including any failures of banks;

- changes in governmental regulations or proposals, or new governmental regulations or proposals, affecting us;

- a continuing recession in the Puerto Rico market and a lack of growth in our other principal markets in the USVI, the BVI and the U.S.;

- the departure of key employees;

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

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

- operating and stock price performance of companies that investors deem comparable to us; and

- the public perception of the banking industry and its safety and soundness.

In addition, the stock market in general, and the NYSE and the other trading markets for the securities of commercial banks and other financial services companies in particular, have experienced significant price and volume fluctuations that sometimes have been unrelated or disproportionate to the operating performance of those companies. These broad market and industry factors may seriously harm the market price of our common stock, regardless of our operating performance or Puerto Rico's economic environment. In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted. A securities class action suit against us could result in substantial costs, potential liabilities and the diversion of management's attention and resources.

Our suspension of dividends may have adversely affected and may further adversely affect our stock price and could result in the expansion of our Board of Directors.

In consideration of the financial results reported for the second quarter ended June 30, 2009, we decided, as a matter of prudent fiscal management and following applicable Federal Reserve Board guidance, to suspend the payment of dividends. The Corporation's ability to declare and pay dividends is dependent on certain Federal regulatory considerations, including the guidelines of the Federal Reserve Board regarding capital adequacy and the approval of the Federal Reserve to declare or pay dividends and receive dividends from the Bank to fund any such dividend payments. In December 2016, for the first time since July 2009, the Corporation paid dividends on its non-cumulative perpetual monthly income preferred stock, after receiving regulatory approval. Since then, the Corporation has continued to paid monthly dividend payments on the non-cumulative perpetual monthly income preferred stock. The Corporation has received regulatory approval to pay monthly dividends on the Corporation's series A through E preferred stock through March 2018. The Corporation intends to continue to request the Federal Reserve's approval to continue to pay the monthly dividends on its Series A through E Preferred Stock.

If the Corporation does not pay dividends in full for eighteen monthly dividend periods (whether consecutive or not), the holders of the Series A through E Preferred Stock as to which dividends have not been paid for eighteen months, acting as a single class, will be entitled to appoint two additional members to our Board of Directors. Any member of the Board of Directors appointed by the holders of Series A through E Preferred Stock is required to vacate his or her office if the Corporation resumes the payment of dividends in full for twelve consecutive monthly dividend periods.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

As of February 16, 2018, First BanCorp. owned the following three main offices located in Puerto Rico:

- Headquarters – Located at First Federal Building, 1519 Ponce de León Avenue, Santurce, Puerto Rico, a 16-story office building. Approximately 51% of the building, an underground three level parking garage and an adjacent parking lot are owned by the Corporation.

- Service Center – a building located on 1130 Muñoz Rivera Avenue, Hato Rey, Puerto Rico. These facilities accommodate branch operations, data processing and administrative and certain headquarter offices. The building houses 180,000 square feet of modern facilities, over 1,000 employees from operations, FirstBank Insurance Agency headquarters and the customer service department. In addition, it has parking for 750 vehicles and 9 training rooms, including classrooms for training tellers and a computer room for interactive trainings, as well as a spacious cafeteria for employees and customers.

- Consumer Lending Center – A three-story building with a three-level parking garage located at 876 Muñoz Rivera Avenue, Hato Rey, Puerto Rico. This facility is fully occupied by the Corporation.

The Corporation owns 19 branch and office premises and parking lots and leases 82 branch premises, loan and office centers and other facilities. In certain situations, financial services such as mortgage and insurance businesses and commercial banking services are located in the same building. All of these premises are located in Puerto Rico, Florida and the USVI and the BVI.

After Hurricane Maria made land fall, the Bank was able to resume operations in Puerto Rico within a week but with some limitations. The Corporation continued normalizing its operations after the hurricanes, and its operations have now substantially returned to pre-hurricane levels. As of the date of the filing of this report, 45 out of 48 FirstBank banking branches in Puerto Rico are providing services, 94% of our network. Certain of the Corporation's facilities and their contents were damaged by these hurricanes and some of the reopened facilities require the replacements of equipment and furnishings. The Corporation has recognized asset impairments of approximately $0.6 million as of December 31, 2017.

Item 3. Legal Proceedings

Reference is made to Note 31, *"Regulatory Matters, Commitments and Contingencies,"* included in the Notes to consolidated financial statements in Item 8 of this Report, which is incorporated herein by reference.

Item 4. Mine Safety Disclosure.

Not applicable.

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 NYSE under the symbol FBP. On February 16, 2018, there were 376 holders of record of the Corporation's common stock, not including beneficial owners whose shares are held in the name of brokers or other nominees. The last sales price for the common stock on that date was $6.23.

Since December 2016, the Corporation has been making monthly dividend payments on the non-cumulative perpetual monthly income preferred stocks which, along with common stock dividend payments, were suspended during the third quarter of 2009. The common stock ranks junior to all series of preferred stock as to dividend rights and as to rights on liquidation, dissolution or winding up of the Corporation.

The following table sets forth, for the periods indicated, the per share high and low closing sales prices for the Corporation's common stock during such periods.

Quarter Ended	High	Low	Last	Dividends per Common Share

2017:								
Fourth Quarter Ended December 31, 2017	$	5.35	$	4.66	$	5.10	$	-
Third Quarter Ended September 30, 2017		6.08		4.97		5.12		-
Second Quarter Ended June 30, 2017		6.12		5.19		5.79		-
First Quarter Ended March 31, 2017		7.00		5.39		5.65		-
2016:								
Fourth Quarter Ended December 31, 2016	$	7.05	$	4.78	$	6.61	$	-
Third Quarter Ended September 30, 2016		5.26		3.82		5.20		-
Second Quarter Ended June 30, 2016		4.62		2.52		3.97		-
First Quarter Ended March 31, 2016		3.23		2.06		2.92		-

On May 10, 2017, the U.S. Department of the Treasury announced that it had sold all of its remaining 10,291,553 shares of the Corporation’s common stock. Since the U.S. Treasury did not recover the full amount of its original investment under TARP, the senior officers forfeited 2,370,571 of their outstanding shares of restricted stock, resulting in a reduction in the number of the Corporation’s common shares outstanding. The U.S. Treasury continues to hold a warrant to purchase 1,285,899 shares of the Corporation’s common stock.

On December 5, 2016, THL and Oaktree completed a secondary offering of the Corporation’s common stock. THL and Oaktree sold an aggregate of 18 million shares (9 million shares each) of common stock at a price of $5.60 per share. In addition, the underwriters exercised their option to purchase an additional 2.7 million shares of common stock from the selling stockholders. Also, on fFebruary 7, 2017, THL and Oaktree participated in a second secondary offering in which they sold an additional aggregate amount of 20 million shares (10 million shares each) of common stock at a price of $6.36 per share. Subsequently, the underwriters exercised their option to purchase an additional 3 million shares of common stock from the selling stockholders. Furthermore, on August 3, 2017, THL and Oaktree participated in a third secondary offering of the Corporation’s common stock in which they sold an aggregate of 20 million shares (10 million shares each) of common stock at a price of $5.70 per share. The Corporation did not receive any proceeds from these offering.

Based on information derived from statements filed with the SEC pursuant to Section 13(d), 13(g) or 16 (a) of the Exchange Act, as of December 31, 2017 each of THL and Oaktree owned less than 5% of the Corporation’s outstanding common stock.

Effective April 1, 2013, the Board determined to increase the salary amounts paid to certain executive officers primarily by paying the increased salary amounts in the form of shares of the Corporation's common stock, instead of cash. The Corporation issued 582,193 shares of common stock with a weighted average market value of $5.64 in 2017 as such additional salary amounts (2016 – 755,223 shares with a weighted average market value of $3.96). The Corporation withheld 195,789 shares from the common stock paid to the officers as additional compensation to cover employee payroll and income tax withholding liabilities in 2017 (2016 – 226,261 shares); these shares are held as treasury shares. The Corporation paid any fractional share of salary stock that the officer was entitled to in cash.

In 2017, the Corporation granted 1,099,756 shares of restricted stock to certain executive officers, other employees, and independent directors (2016 – 1,925,575 shares). In connection with the vesting of restricted stock in 2017, the Corporation withheld 243,102 shares of restricted stock (2016 – 65,498 shares) to cover employee payroll and income tax withholding liabilities; these shares are also held as treasury shares.

As of December 31, 2017 and December 31, 2016, the Corporation had 4,104,303 and 1,254,189 shares held as treasury stock, respectively.

The Corporation has 50,000,000 authorized shares of preferred stock. First BanCorp. has five outstanding series of nonconvertible, noncumulative preferred stock: 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); and 7.00% noncumulative perpetual monthly income preferred stock, Series E (liquidation preference $25 per share) (collectively, the "Series A through E Preferred Stock"). Effective January 17, 2012, the Corporation delisted all of its outstanding series of preferred stock from the NYSE. The Corporation has not arranged for listing on another national securities exchange or for quotation of the Series A through E Preferred Stock in a quotation medium.

The Series A through E Preferred Stock rank on a 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 terms of the Corporation's Series A through E 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; 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 through E Preferred Stock, except with the consent of the holders of at least two-thirds of the outstanding aggregate liquidation preference of such preferred stock.

Dividends

The Corporation had a policy of paying quarterly cash dividends on its outstanding shares of common stock subject to its earnings and financial condition. For the first time since July 2009, following the requisite regulatory approval, on December 8, 2016, the Corporation announced the declaration of a cash dividend on its outstanding shares of Series A through E Noncumulative Perpetual Monthly Income Preferred Stock for the month of December 2016. Since then, the Corporation has continued to pay monthly dividend payments on the non-cumulative perpetual monthly income preferred stock. The Corporation has received regulatory approval to pay the monthly dividends on the Corporation's Series A through E Preferred Stock through March 2018. 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.

On October 3, 2017, the Federal Reserve terminated the Written Agreement entered to on June 3, 2010 between the Corporation and the Federal Reserve. However, the Corporation has agreed with the its regulators to continue to obtain approval before paying dividends, receiving dividends from the Bank, making payments on subordinated debt or trust preferred securities, incurring or guaranteeing debt or purchasing or redeeming any corporate stock.

The 2011 PR Code requires the withholding of income taxes from dividend income sourced within Puerto Rico to be received by any individual, resident of Puerto Rico or not, trusts and estates and by non-resident custodians, partnerships, and corporations.

Resident U.S. Citizens

A special tax of 15% withheld at source is imposed, in lieu of regular tax, on any eligible dividends paid to individuals, trusts, and estates. Eligible dividends include dividends paid by a domestic Puerto Rico corporation. However, the taxpayer can perform an election to be excluded from the 15% special tax. Once this election is made it is irrevocable. The election allows the taxpayer to include in gross income the eligible dividends received and take a credit for the amount of tax withheld in excess, if any. If the taxpayer does not make this election on the tax return, then he can exclude from gross income the eligible dividends 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 15% 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 a trade or business in Puerto Rico during the taxable year in which the dividend, if any, 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 a trade or business in Puerto Rico are not subject to the 10% withholding, but they must declare any dividend as gross income on their Puerto Rico income tax return.

Securities authorized for issuance under equity compensation plans

The following table summarizes equity compensation plans approved by security holders and equity compensation plans that were not approved by security holders as of December 31, 2017:

Plan category	(a) Number of Securities to be Issued Upon Exercise of Outstanding Options, warrants and rights	(b) Weighted Average Exercise Price of Outstanding Options, warrants and rights	(c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
Equity compensation plans, approved by stockholders	-	$ -	7,558,450(1)
Equity compensation plans not approved by stockholders	N/A	N/A	N/A
Total	-	$ -	7,558,450

(1) Securities available for future issuance under the First BanCorp. 2008 Omnibus Incentive Plan (the "Omnibus Plan"), which was initially approved by stockholders on April 29, 2008. Most recently, on May 24, 2016, the Omnibus Plan was amended to, among other things, increase the number of shares of common stock reserved for issuance under the Omnibus Plan, to extend the term of the Omnibus Plan to May 24, 2026 and to re-approve the material terms of the performance goals under the Omnibus Plan for purpose of Section 162(m) of the U.S. Internal Revenue Code of 1986, as amended. The Omnibus Plan provides for equity-based compensation incentives through the grant of stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, and other stock-based awards. As amended, this plan provides for the issuance of up to 14,169,807 shares of common stock, subject to adjustments for stock splits, reorganization and other similar events. As of December 31, 2017, 7,558,450 shares of Common Stock were available for future issuance under the Omnibus Plan.

Purchase of equity securities by the issuer and affiliated purchasers

The following table provides information relating to the Corporation's purchases of shares of its common stock in the three-month period ended December 31, 2017:

Period	Total number of shares purchased (1)	Average Price Paid	Total Number of Shares Purchased as Part of Publicly Announced Plans Or Programs	Maximum Number of Shares That May Yet be Purchased Under These Plans or Programs
October, 2017	17,343	$ 4.99	-	-

November, 2017	17,850		4.85	-	-
December, 2017	17,087		5.07	-	-
Total	52,280	$	4.97	-	-

(1) Reflects shares of common stock withheld from the common stock paid to certain senior officers.

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 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, 2012 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, 2012 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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Item 6. Selected Financial Data

The following table sets forth certain selected consolidated financial data for each of the five years in the period ended December 31, 2017. This information should be read in conjunction with the audited consolidated financial statements and the related notes thereto.

SELECTED FINANCIAL DATA

	Year Ended December 31,				
(In thousands, except for per share and financial ratios)	**2017**	**2016**	**2015**	**2014**	**2013**
Condensed Income Statements:					
Total interest income	$ 588,423	$ 585,292	$ 605,569	$ 633,949	$ 645,78
Total interest expense	96,872	101,174	103,303	115,876	130,84
Net interest income	491,551	484,118	502,266	518,073	514,94
Provision for loan and lease losses	144,254	86,733	172,045	109,530	243,75
Non-interest income (loss)	62,387	87,954	81,325	61,348	(15,48
Non-interest expenses	347,701	355,080	383,830	378,253	415,02
Income (loss) before income taxes	61,983	130,259	27,716	91,638	(159,32
Income tax benefit (expense)	4,973	(37,030)	(6,419)	300,649	(5,16
Net income (loss)	66,956	93,229	21,297	392,287	(164,48
Net income (loss) attributable to common stockholders - basic	64,280	93,006	21,297	393,946	(164,48
Net income (loss) attributable to common stockholders - diluted	64,280	93,006	21,297	393,946	(164,48
Per Common Share Results:					
Net earnings (loss) per common share - basic	$ 0.30	$ 0.44	$ 0.10	$ 1.89	$ (0.8
Net earnings (loss) per common share - diluted	$ 0.30	$ 0.43	$ 0.10	$ 1.87	$ (0.8
Cash dividends declared	-	-	-	-	
Average shares outstanding	213,963	212,818	211,457	208,752	205,54
Average shares outstanding diluted	216,118	215,794	212,971	210,540	205,54
Book value per common share	$ 8.48	$ 8.05	$ 7.71	$ 7.68	$ 5.5
Tangible book value per common share (1)	$ 8.28	$ 7.83	$ 7.47	$ 7.45	$ 5.3
Balance Sheet Data:					
Total loans, including loans held for sale	$ 8,883,456	$ 8,936,879	$ 9,148,251	$ 9,177,371	$ 9,545,50
Allowance for loan and lease losses	231,843	205,603	240,710	222,395	285,85
Money market and investment securities	2,095,177	2,091,196	2,299,520	2,170,401	2,374,98
Intangible assets	42,351	46,754	50,583	49,907	54,86
Deferred tax asset, net	294,809	281,657	311,263	313,045	7,64
Total assets	12,261,268	11,922,455	12,573,019	12,727,835	12,656,92
Deposits	9,022,631	8,831,205	9,338,124	9,483,945	9,879,92
Borrowings	1,223,635	1,186,187	1,381,492	1,456,959	1,431,95
Total preferred equity	36,104	36,104	36,104	36,104	63,04
Total common equity	1,853,608	1,784,529	1,685,779	1,653,990	1,231,54
Accumulated other comprehensive loss, net of tax	(20,615)	(34,390)	(27,749)	(18,351)	(78,73
Total equity	1,869,097	1,786,243	1,694,134	1,671,743	1,215,85

	Year Ended December 31,				
	2017	**2016**	**2015**	**2014**	**2013**
Selected Financial Ratios (In Percent):					
Profitability:					
Return on Average Assets	0.56	0.75	0.17	3.10	(1.28)
Return on Average Total Equity	3.63	5.28	1.26	30.25	(12.39)
Return on Average Common Equity	3.71	5.39	1.29	31.38	(13.01)
Average Total Equity to Average Total Assets	15.39	14.25	13.23	10.25	10.36
Interest Rate Spread	4.07	3.88	3.94	4.02	3.92
Interest Rate Margin	4.36	4.14	4.15	4.20	4.11
Interest Rate Spread - tax equivalent basis (2)	4.22	3.99	4.08	4.16	4.01
Interest Rate Margin - tax equivalent basis (2)	4.51	4.25	4.30	4.34	4.21
Tangible common equity ratio (1)	14.65	14.34	12.84	12.51	8.71
Dividend payout ratio	-	-	-	-	-
Efficiency ratio (3)	62.77	62.07	65.77	65.28	83.10
Asset Quality:					
Allowance for loan and lease losses to loans held for investment	2.62	2.31	2.64	2.44	3.02
Net charge-offs to average loans (4)	1.33	1.37	1.68	1.84	4.07
Provision for loan and lease losses to net charge-offs	1.22x	0.71x	1.12x	0.63x	0.69x
Non-performing assets to total assets (4)	5.31	6.16	4.85	5.63	5.73
Non-performing loans held for investment to total loans held for investment (4)	5.53	6.30	4.86	5.76	5.23
Allowance to total non-performing loans held for investment	47.36	36.71	54.36	42.45	57.69
Allowance to total non-performing loans held for investment, excluding residential real estate loans	74.48	51.50	87.92	64.80	85.56
Other Information:					
Common stock price: End of period	$ 5.10	$ 6.61	$ 3.25	$ 5.87	$ 6.19

(1) Non-GAAP financial measures. Refer to "Capital" below for additional information about the components and a reconciliation of these measures.

(2) On a tax-equivalent basis and excluding the changes in the fair value of derivative instruments (see "Net Interest Income" below for a reconciliation of these non-GAAP financial measures).

(3) Non-interest expenses to the sum of net interest income and non-interest income.

(4) Loans used in the denominator in calculating each of these ratios include purchased credit-impaired loans. However, the Corporation separately tracks and reports purchased credit-impaired loans and excludes these from non-performing loan and non-performing asset amounts.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A)

The following Management's Discussion and Analysis of Financial Condition and Results of Operations relates to the accompanying audited consolidated financial statements of First BanCorp. and should be read in conjunction with such financial statements and the notes thereto. This section also presents certain non-GAAP financial measures. Refer to *Basis of Presentation* below for information about why the non-GAAP financial measures are being presented and the reconciliation of the non-GAAP financial measures for which the reconciliation is not presented earlier.

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 and FirstBank Insurance Agency. Through its wholly-owned subsidiaries, the Corporation operates offices in Puerto Rico, the United States Virgin Islands and British Virgin Islands, and the State of Florida (USA), concentrating on commercial banking, residential mortgage loan originations, finance leases, credit cards, personal loans, small loans, auto loans, and insurance agency and broker-dealer activities.

NATURAL DISASTERS AFFECTING FIRST BANCORP. IN 2017

Two strong hurricanes affected the Corporation's service areas during 2017. Early in September, Hurricane Irma, a Category 5 hurricane, affected the eastern Caribbean islands, including the U.S. Virgin Islands of St. Thomas and St. John and Tortola in the British Virgin Islands, and, to a lesser extent, the U.S. Virgin Island of St. Croix and Puerto Rico. After hitting the eastern Caribbean, Hurricane Irma made landfall along Florida's southwest shoreline. Two weeks after Hurricane Irma sideswiped Puerto Rico, Hurricane Maria made landfall in the south-east corner of Puerto Rico as a Category 4 hurricane and exited on the northern coast at a point between the cities of Arecibo and Barceloneta after battering other islands in the Caribbean, including St. Croix. These hurricanes caused widespread property damage, flooding, power outages, and water and communication services interruptions, and have severely disrupted normal economic activity in all of these regions.

The following summarizes the more significant financial repercussions of these natural disasters for the Corporation and for its major subsidiary, FirstBank:

Credit Quality and Allowance for Loan and Lease Losses

As of the end of the third quarter of 2017, the Corporation established a $66.5 million allowance for loan and lease losses directly related to the initial estimate, based on available information, of inherent losses resulting from the impact of the storms. During the fourth quarter of 2017, loan officers performed reviews of the storms' impact on large commercial borrowers, and the results of these reviews were factored into the determination of the allowance for loan and lease losses as of December 31, 2017. The Corporation recorded an incremental provision expense of $4.8 million during the fourth quarter of 2017, primarily related to higher than initial estimated losses associated with the effects of the hurricanes on its commercial and construction loan portfolios. The storm-related allowance as of December 31, 2017 amounted to $68.5 million (net of a $2.8 million charge off taken on a storm-impacted credit during the fourth quarter of 2017). The Corporation's approach to estimating the storms' impact on credit quality is discussed in the *Provision for Loan and Lease Losse*s section below.

Interruptions in regular collection efforts caused by Hurricanes Irma and Maria adversely affected the Corporation's non-performing loan statistics. Non-performing residential mortgage loans increased in the second half of 2017 by $23.0 million to $178.3 million as of December 31, 2017 and non-performing commercial and construction loans held for investment increased in the second half of 2017 by $59.4 million to $294.4 million as of December 31, 2017. Refer to *Risk Management – Non-performing Loans and Non-performing Assets* section below for additional information about early delinquency statistics and payment deferral programs established by the Corporation to assist individuals and businesses affected by the recent storms.

Disaster Response Plan Costs, Casualty Losses and Related Insurance

The Corporation implemented its disaster response plan as these hurricanes approached its service areas. To operate in disaster response mode, the Corporation incurred expenses for, among other things, buying diesel and generators for electric power, debris removal, security matters, and emergency communications with customers regarding the status of Bank operations. The disaster response plan costs, combined with payroll and rental costs during the idle time caused by the hurricanes, totaled $6.6 million as of December 31, 2017.

The Bank was able to resume operations in Puerto Rico within a week after Hurricane Maria made landfall, but with some limitations. The Corporation continued normalizing its operations after the hurricanes and its operations have now substantially returned to pre-hurricane levels. As of the date of the filing of this report, 45 out of 48 FirstBank banking branches in Puerto Rico are providing services and connected to the electrical grid, 94% of our network In addition, 82 of our ATMs are operational, 98% of our network, plus 82 of the ATMs that are offered through a third party alliance. Certain of the Corporation's facilities and their contents were damaged by these hurricanes and some of the reopened facilities require the replacements of equipment and furnishings. The Corporation has recognized asset impairments of approximately $0.6 million as of December 31, 2017.

The Corporation maintains insurance for casualty losses as well as for disaster response costs and certain revenue lost through business interruption. Management believes, based on its understanding of the insurance coverages, that recovery of $4.8 million of the $7.2 million above-mentioned costs and asset impairments identified as of December 31, 2017 is probable. Accordingly, as of December 31, 2017, a receivable of $4.8 million was included in the consolidated statement of financial condition as part of "Other assets" for the expected recovery. Non-interest expenses for 2017 reflect approximately $2.5 million of insurance deductibles related to damages assessed on certain OREO properties and estimated storm-related costs not recoverable under insurance policies. Management also believes that there is a possibility that some gains will be recognized with respect to casualty and lost revenue claims in future periods, but this is contingent on reaching agreement on the Corporation's claims with the insurance carriers.

Liquidity Management

The Corporation experienced rapid accumulation of deposits after the hurricanes. Total deposits as of December 31, 2017, excluding brokered CDs, increased by $361.5 million from September 30, 2017. The most significant increase was in noninterest-bearing demand deposits, which grew 16%, or $247.5 million, during the fourth quarter of 2017. Storm-related factors, such as the effect of the payment deferral programs and disaster relief funds, contributed to this accumulation. Although management expects the balances accumulated by deposit customers in the storm-affected areas to reduce over time, it is difficult to predict when and to what degree, and there may be some further growth as insurance claims are resolved and additional disaster-recovery funds are distributed. Funds from the deposit build-up were primarily deposited at the Federal Reserve Bank, pending better information on the volatility of these funds.

EXECUTIVE Overview of Results of Operations

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

The Corporation had net income of $67.0 million, or $0.30 per diluted share, for the year ended December 31, 2017, compared to $93.2 million, or $0.43 per diluted share, for 2016 and $21.3 million, or $0.10 per diluted share, for 2015. The Corporation's financial results for 2017, 2016, and 2015 included the following items that management believes are not reflective of core operating performance, are not expected to reoccur with any regularity or may reoccur at uncertain times and in uncertain amounts (the "Special Items"):

<u>Year ended December 31, 2017</u>

- Charges of $73.9 million ($45.1 million after-tax) related to the effect of Hurricanes Irma and Maria, which includes the following items: (i) a $71.3 million charge to the provision for loan and lease losses directly related to the estimate of inherent losses resulting from the effects of the storms, and (ii) $2.5 million of non-interest expenses associated with insurance deductibles related to damages assessed on certain OREO properties and estimated storm-related costs not recoverable under insurance policies. The $73.9 million impact was partially offset in the consolidated financial results by expected insurance recoveries of $1.9 million for compensation and rental costs that the Corporation incurred when Hurricanes Irma and Maria precluded employees from working during 2017.

- Tax benefit of $13.2 million associated with the change in tax status of certain subsidiaries from taxable corporations to limited liability companies that make an election to be treated as partnerships for income tax purposes in Puerto Rico. Refer to the *Income Taxes* discussion below for additional information.

- OTTI charge of $12.2 million and a $0.4 million recovery of previously recorded OTTI charges on non-performing bonds of the GDB and the Puerto Rico Public Buildings Authority sold in 2017. No tax benefit was recognized for the OTTI charge and the recovery on the sale of the bonds. Refer to the *Exposure to Puerto Rico Government* discussion below for additional information.

• Gain of $1.4 million on the repurchase and cancellation of $7.3 million in trust-preferred securities, reflected in the consolidated statements of income as “Gain on early extinguishment of debt.” The gain, realized at the holding company level, had no effect on the income tax expense in 2017. Refer to the *Non-Interest Income* discussion below for additional information.

• Charge of $0.6 million to the provision for loan and lease losses ($0.3 million after-tax) associated with the sale of the Corporation’s participation in the PREPA credit line with a book value of $64 million at the time of sale. Refer to the *Provision for Loan and Lease Losses* discussion below for additional information.

• Costs of $0.4 million associated with the secondary offerings of the Corporation’s common stock by certain of our existing stockholders in 2017. The costs, incurred at the holding company level, had no effect on the income tax expense in 2017.

<u>Year ended December 31, 2016</u>

• OTTI charges of $6.7 million on debt securities, primarily on the aforementioned bonds of the GDB and the Puerto Rico Public Buildings Authority. No tax benefit was recognized for the OTTI charges in 2016.

• Gain of $6.1 million ($5.9 million after-tax) on sales of $198.7 million of U.S. agency mortgage-backed securities (“MBS”) that carried an average yield of 2.36%.

• Gain of $4.2 million on the repurchase and cancellation of $10 million in trust-preferred securities, reflected in the consolidated statements of income as “Gain on early extinguishment of debt.” The gain, realized at the holding company level, had no effect on the income tax expense in 2016.

• Adjustment of $2.7 million ($1.7 million after tax) recorded to reduce the credit card rewards program liability due to the expiration of reward points earned by customers up to September 2013 (the conversion date of the credit card portfolio acquired from FIA in May 2012). Most of these points had been accrued at the acquisition date and ultimately experienced a redemption pattern materially different from those points accrued after the conversion

- Charge to the provision for loan and lease losses of $1.8 million ($1.1 million after-tax) related to the sale of a $16.3 million pool of non-performing assets, mostly comprised of non-performing commercial loans.

- Brokerage and insurance commissions of $1.7 million ($1.0 million after-tax) net of incentive costs, primarily from the sale of large fixed annuities contracts.

- Gain of $1.5 million ($1.2 million after-tax) from recovery of a residual collateralized mortgage obligation ("CMO") previously written off.

- Costs of $0.6 million associated with a secondary offering of the Corporation's common stock by certain of the existing stockholders. The costs, incurred at the holding company level, had no effect on the income tax expense in 2016.

- Severance payments of $0.3 million ($0.2 million after-tax) related to permanent job discontinuance recorded in 2016.

Year ended December 31, 2015

- Charges of $48.7 million ($29.7 million after-tax) related to a bulk sale of assets with a carrying value of $150.4 million (the "bulk sale of assets") completed in 2015, mostly comprised of non-performing commercial loans. The charges of $48.7 million include the following items: (i) a $46.9 million charge to the provision for loan and lease losses, (ii) non-interest expenses of $1.2 million directly associated with the bulk sale of assets, and (iii) a $0.6 million loss recorded as part of non-interest income in the consolidated statements of income associated with loans held for sale included in the bulk sale of assets.

- OTTI charges of $16.5 million on debt securities, primarily on the aforementioned bonds of the GDB and the Puerto Rico Public Buildings Authority. No tax benefit was recognized for the OTTI charges in 2015.

- Bargain purchase gain of $13.4 million ($8.2 million after-tax) on assets acquired and liabilities assumed from Doral Bank in 2015.

- Gain of $7.0 million ($4.3 million after-tax) associated with a long-term strategic marketing alliance entered into during 2015 as part of the sale of the FirstBank Puerto Rico merchant contracts portfolio.

- Costs of $4.6 million ($2.8 million after-tax) related to the conversion of loan and deposit accounts acquired from Doral Bank to the FirstBank systems.

- Costs of $2.2 million ($1.4 million after-tax) related to a voluntary early retirement program recorded in 2015.

The following table reconciles for 2017, 2016, and 2015 the reported net income to adjusted net income, a non-GAAP financial measure that excludes the Special Items identified above:

	Year Ended December 31,		
	2017	**2016**	**2015**
(In thousands)			
Net income, as reported (GAAP)	$ 66,956	$ 93,229	$ 21,297
Adjustments:			
Storm-related provision for loan and lease losses	71,304	-	-
Storm-related expenses	2,544	-	-
Idle time payroll and rental costs insurance recovery	(1,819)	-	-
Charge to the provision related to the sale of the $16.3 million pool of non-performing assets	-	1,799	-
Charges related to the bulk sale of assets, including transaction expenses	-	-	48,667
Gain from recovery of investments previously written off	-	(1,547)	-
Brokerage and insurance commissions, primarily from the sale of large fixed annuities contracts, net of incentive costs	-	(1,692)	-
Adjustment to reduce the credit cards rewards liability due to unusually large customer forfeitures	-	(2,732)	-
Charge to the provision related to the sale of the PREPA credit line	569	-	-
Secondary offering costs	392	590	-
Gain on sale of investment securities	-	(6,104)	-
Severance payments on jobs discontinuance	-	281	-
OTTI on debt securities	12,231	6,687	16,517
Gain on early extinguishment of debt	(1,391)	(4,217)	-
Gain on sale of merchant contracts	-	-	(7,000)
Voluntary early retirement program expenses	-	-	2,238

Bargain purchase gain on assets acquired and liabilities assumed from Doral Bank	-	-	(13,443)
Acquisition and conversion costs of assets acquired and liabilities assumed from Doral Bank	-	-	4,646
Income tax benefit related to change in tax-status of certain subsidiaries	(13,161)	-	-
Recovery of previously recorded OTTI charges on Puerto Rico government debt securities sold	(371)	-	-
Income tax impact of adjustments (1)	(28,906)	1,409	(13,691)
Adjusted net income	$ 108,348	$ 87,703	$ 59,231

(1) See "Basis of Presentation" for the individual tax impact for each reconciling item.

The key drivers of the Corporation's GAAP financial results include the following:

- Net interest income for the year ended December 31, 2017 was $491.6 million compared to $484.1 million and $502.3 million for the years ended December 31, 2016 and 2015, respectively. The increase for 2017 compared to 2016 was primarily driven by: (i) a $12.5 million increase in interest income on commercial and construction loans, primarily associated with both the upward repricing of variable-rate commercial loans and the growth of the performing commercial portfolios, primarily in the Florida region; (ii) a $4.3 million decrease in interest expense, including a decrease of $2.8 million in interest expense on brokered CDs primarily related to a $509.0 million decrease in the average balance of brokered CDs that offset higher costs on new issuances, and a $9.3 million decrease in interest expense on repurchase agreements primarily reflecting the full-year effect of the repayment of $400 million of repurchase agreements that matured in the third and fourth quarters of 2016 and carried an average cost of 3.35%, partially offset by increases of $5.2 million and $2.0 million in interest expense on FHLB advances and non-brokered deposits, respectively; and (iii) a $1.2 million increase in interest income from deposits maintained at the Federal Reserve Bank due to increases in the Federal Funds target rate in 2017 and late in 2016.

The aforementioned variances were partially offset by: (i) a $5.6 million decrease in interest income on consumer loans and finance leases, primarily reflecting a $33.5 million decrease in the average balance of this portfolio, primarily auto loans, and, to a lesser extent, the effect of a $1.4 million decrease in late payment fees as the Corporation did not assess late charges during the fourth quarter of 2017 to customers affected by Hurricanes Irma and Maria that qualified for the three-month payment deferral program established by the Corporation after the hurricanes, and (ii) a $5.3 million decrease in interest income on residential mortgage loans, reflecting both a higher level of inflows of residential mortgage loans to non-performing status and a $41.8 million decrease in the average balance of this portfolio.

The net interest margin increased to 4.36% for the year ended December 31, 2017 compared to 4.14% for 2016, primarily due to the aforementioned upward repricing of commercial and construction loans, a lower U.S. agency MBS premium amortization expense resulting from lower prepayment rates in 2017, and the benefit of the overall lower level of liquidity that reflects the effect of cash balances used for the repayment of high-cost repurchase agreements that matured in the second half of 2016.

The decrease for 2016 compared to 2015 was primarily driven by: (i) a $15.2 million decrease in interest income on consumer loans and finance leases mainly attributable to a decrease of $142.8 million in the average balance of this portfolio, primarily auto loans; (ii) a $3.9 million decrease in interest income on investment securities, primarily reflecting the gradual reinvestment of MBS prepayments in lower yielding securities given the low interest rate environment that prevailed in 2016 and an adverse impact of approximately $1.0 million related to the discontinuance of interest income recognition on bonds of the GDB and the Puerto Rico Public Buildings Authority that were placed in non-performing status in the third quarter of 2016; (iii) a $1.2 million decrease in interest income on commercial and construction loans, reflecting a decline of $153.4 million in the average balance of these portfolios that resulted in a decrease of approximately $3.6 million in interest income and the adverse impact of large commercial relationships classified as non-performing during 2016, partially offset by an increase of approximately $1.4 million in prepayment penalties and deferred fees amortization, recovery of interest income on certain non-performing loans that were fully paid off, and the upward repricing of variable commercial loans tied to higher short-term interest rates; and (iv) a $1.2 million decrease in interest income on residential mortgage loans primarily due to lower cash collections on residential non-performing loans.

These variances were partially offset by: (i) a $2.1 million decrease in interest expense, including a decrease of $3.0 million in interest expense on brokered CDs primarily related to a $622.7 million decrease in the average volume of brokered CDs that offset higher costs on new issuances, and a $2.2 million decrease in interest expense on repurchase agreements, primarily reflecting the effect of the repayment of $400 million of repurchase agreements that matured in 2016 and carried an average cost of 3.35%, partially offset by increases of $1.8 million and $1.0 million in interest expense on FHLB advances and non-brokered deposits, respectively; and (ii) a $1.2 million increase in interest income on interest-bearing cash and cash equivalent balances due to increases in fed fund rates late in 2015 and 2016. The net interest margin decreased slightly to 4.14% for the year ended December 31, 2016 compared to 4.15% for 2015.

- The provision for loan and lease losses for 2017 was $144.3 million compared to $86.7 million and $172.0 million for 2016 and 2015, respectively. These provisions included the following: for the year ended December 31, 2017, a charge of $71.3 million directly related to the estimate of inherent losses resulting from the effects of Hurricanes Irma and Maria and a $0.6 million charge associated with the sale of the PREPA credit line; for 2016 a charge of $1.8 million associated with the sale of a $16.3 million pool of non-performing assets; and for 2015, a charge of $46.9 million associated with the bulk sale of assets discussed below. Excluding the effect of the aforementioned items, the adjusted provision for loan and lease losses of $72.4 million for 2017 decreased by $12.6 million compared to the adjusted provision for loan and lease losses of $84.9 million for 2016 reflecting; (i) a $20.8 million decrease in the adjusted provision for commercial and construction loans reflecting, among other things, lower specific reserve requirements for impaired loans and a $2.9 million increase in loan loss recoveries; and (ii) a $2.8 million decrease in the adjusted provision for consumer loans and finance leases, mainly related to lower levels of personal and small loans delinquencies. These variances were partially offset by an $11.1 million increase in the adjusted provision for residential mortgage loans, primarily related to a higher level of residential non-performing loans, increased specific reserves for residential mortgage TDRs, and higher loss severity estimates in 2017.

The adjusted provision for loan and lease losses of $84.9 million for the year ended December 31, 2016 decreased by $40.2 million compared to the adjusted provision for loan and lease losses of $125.1 million for 2015 reflecting; (i) a $23.2 million decrease in the adjusted provision for commercial and construction loans reflecting, among other things, the impact in 2015 of the $35 million increase in the general reserve for commercial loans extended to or guaranteed by the Puerto Rico government (excluding municipalities), reflecting both the migration of certain of these loans to adverse classification categories and a $19.2 million charge related to qualitative factor adjustments that stressed the historical loss rates applied to these loans, partially offset by lower loan loss recoveries and, the impact in 2015 of an $8.1 million reserve release adjustment for construction loans that reflected adjustments to the general reserve given the stabilization in the asset quality of land loans; (ii) an $11.7 million decrease in the provision for consumer loans, driven by lower charge-offs and loss severity rates and the overall decrease in the size of this portfolio; and (iii) a $5.3 million decrease in the adjusted provision for residential mortgage loans mainly related to lower delinquency levels, lower charges to the reserve for PCI loans, and the overall decrease in the size of this portfolio.

Refer to *Basis of Presentation* below for additional information and reconciliation of the provision for loan and lease losses in accordance with GAAP to the non-GAAP adjusted provision for loan and lease losses.

Net charge-offs totaled $118.0 million for the year ended December 31, 2017, or 1.33% of average loans, including a $10.7 million charge-off associated with the sale of the PREPA credit line. Net charge-offs for the year ended December 31, 2016 totaled $121.8 million, or 1.37% of average loans, including $4.6 million of net charge-offs related to the sale of a $16.3 million pool of non-performing assets. Net charge-offs for the year ended December 31, 2015 totaled $153.7 million, or 1.68% of average loans, including $61.4 million of net charge-offs related to the bulk sale of assets in 2015. Adjusted net charge-offs that exclude from net charge-offs for 2017 the impact of the sale of the PREPA credit line, for 2016, the impact of the sale of the $16.3 million of non-performing assets, and for 2015, the impact of the bulk sale of assets are non-GAAP financial measures. Non-GAAP adjusted net charge-offs for 2017 amounted to $107.3 million, or 1.21% of average loans, a decrease of $9.9 million compared to non-GAAP adjusted net charge-offs of $117.2 million for 2016. The decrease in 2017, compared to 2016, reflects reductions of $18.9 million, $9.7 million, and $4.9 million in adjusted charge-offs taken on commercial and industrial, consumer, and residential mortgage loans, respectively, partially offset by a $16.8 million increase in charge-offs taken on TDF commercial mortgage loans. Refer to *Basis of Presentation* below for additional information about these non-GAAP financial measures. Also refer to the discussions under *Provision for loan and lease losses* and *Risk Management* below for an analysis of the allowance for loan and lease losses and non-performing assets and related ratios.

- The Corporation recorded non-interest income of $62.4 million for the year ended December 31, 2017 compared to $88.0 million and $81.3 million for the years ended December 31, 2016 and 2015, respectively. The decrease for 2017 compared to 2016 was primarily driven by: (i) a $6.9 million decrease in revenues from mortgage banking activities, primarily due to lower conforming loan origination and sales volume associated with both the drop in business activity in Puerto Rico and the Virgin Islands after the hurricanes and higher market interest rates; (ii) the effect in 2016 of a $6.1 million gain on sales of $198.7 million of U.S. agency MBS; (iii) a $5.9 million increase in OTTI charges on bonds of the GDB and the Puerto Rico Public Buildings Authority; (iv) a $2.9 million decrease in gains associated with repurchases and cancellations of trust-preferred securities; (v) the effect in 2016 of a $1.5 million gain from the recovery of a residual CMO previously written off; and (vi) the effect in 2016 of brokerage and insurance commissions of $1.8 million, primarily related to the sale of large fixed annuities contracts.

The increase of $6.7 million for 2016 compared to 2015 was primarily driven by: (i) a $9.8 million decrease in OTTI charges on debt securities, primarily related to lower charges on bonds of the GDB and the Puerto Rico Public Buildings Authority; (ii) a $6.1 million gain on sales of $198.7 million of U.S. agency MBS in 2016; (iii) a $4.2 million gain on the repurchase and cancellation of $10 million in trust-preferred securities in 2016; (iv) a $3.2 million increase in revenues from the mortgage banking business, driven by higher gains on sales of residential mortgage loans in the secondary market associated with both a higher volume of sales and higher gain margins; (v) a $2.6 million increase in service charges on deposits primarily related to the implementation of new service and transactional fees on certain products in November 2015; (vi) a $2.2 million increase in insurance and broker-dealer commissions, primarily related to the sale of large fixed annuities contracts; and (viii) a $1.5 million gain from the recovery of a residual CMO previously written off. These increases were partially offset by the effect in 2015 of the $13.4 million bargain purchase gain on assets acquired and liabilities assumed from Doral Bank and the effect in 2015 of a $7.0 million gain on the sale of merchant contracts.

- Non-interest expenses for 2017 were $347.7 million compared to $355.1 million and $383.8 million for 2016 and 2015, respectively. The decrease for 2017 compared to 2016 was primarily due to: (i) a $6.3 million decrease in the FDIC insurance premium expense, mainly related to the effect of reductions in brokered deposits and average assets, a strengthened capital position, and improved liquidity metrics; (ii) a $2.1 million decrease in the provision for unfunded loan commitments and letters of credit; (iii) a $0.8 million decrease in write-downs, loss on sales and expenses related to non-real estate repossessed assets; (iv) a $0.6 million decrease in communications-related matters such as telephone and postage expenses; (v) a $0.6 million decrease in taxes, other than income taxes, primarily related to decreases in the sales and use tax expense and in municipal license taxes in Puerto Rico; (vi) a $0.5 million decrease in losses from OREO operations, primarily reflecting a $1.8 million decrease in write-downs to the value of OREO properties, partially offset by a $1.2 million decrease in rental income from commercial OREO income-producing properties; and (vii) a $0.4 million decrease in credit and debit card processing expenses, primarily associated with a lower volume of transactions affected by the drop in business activity after the hurricanes in 2017. These variances were partially offset by: (i) a $1.8 million increase in professional service fees, primarily reflecting higher consulting fees related to the implementation of new technology systems and higher outsourcing fees related to network services; (ii) a $1.5 million increase in occupancy and equipment costs, primarily due to higher electricity expenses, property taxes and rental expenses; (iii) a $1.1 million increase in business promotion expenses, reflecting the effect in 2016 of a $2.7 million adjustment recorded to reduce the credit card rewards program liability due to the expiration of reward points earned by customers up to September 2013 (the conversion date of the credit card portfolio acquired from FIA in May 2012) and costs of approximately $1.0 million related to hurricane relief efforts and assistance to employees incurred in 2017, partially offset by a $1.3 million decrease associated with lower advertising and marketing-related activities. Adjusted non-interest expenses, which exclude Special Items, were $346.6 million for 2017, compared to adjusted non-interest expenses of $356.9 million in 2016. Refer to *Basis of Presentation* below for additional information and reconciliation of this non-GAAP financial measure.

The decrease for 2016 compared to 2015 was primarily due to: (i) an $11.5 million decrease in total professional service fees, mainly driven by the effect in 2015 of several items, including, professional services fees of $3.7 million related to the acquisition and conversion of loan and deposit accounts acquired from Doral Bank to the FirstBank systems, $3.6 million of interim servicing costs related to loans and deposits acquired from Doral Bank, costs of $1.3 million related to special projects and strategic, stress testing and capital planning matters, professional service fees of $0.9 million directly related to the bulk sale of assets, and a $2.9 million decrease in collections, appraisals and other credit related professional service fees associated with lower costs on troubled loans resolution efforts; (ii) a $4.3 million decrease in losses on OREO operations, primarily reflecting decreases in write downs to the value of OREO properties and in OREO-operating expenses, including lower property taxes, and an increase in rental income; (iii) a $4.1 million decrease in occupancy and equipment costs reflecting reductions in depreciation, electricity and repairs expenses; (iv) a $3.9 million decrease in the FDIC insurance premium expense reflecting, among other things, a reduction in the initial base assessment rate, and reductions in brokered deposits and average assets; (v) a $3.8 million decrease in business promotion expenses, primarily due to lower costs associated with credit card and deposit reward programs, including the effect of the $2.7 million adjustment recorded during the fourth quarter of 2016 to reduce the credit card rewards liability due to the aforementioned expiration of reward points earned by customers up to September 2013; and (vi) a $2.5 million decrease in processing expenses mainly due to the sale of merchant contracts in the fourth quarter of 2015. These variances were partially offset by a $2.5 million increase in taxes, other than income taxes, primarily due to the increase in the sales tax rate from 7% to 11.5%, effective in Puerto Rico since July 1, 2015 and the sales tax of 4% on designated professional services, effective in Puerto Rico since October, 1, 2015. Adjusted non-interest expenses, which exclude Special Items, were $356.9 million for 2016, compared to adjusted non-interest expenses of $375.8 million in 2015. Refer to *Basis of Presentation* below for additional information and reconciliation of this non-GAAP financial measure.

- For 2017, the Corporation recorded an income tax benefit of $5.0 million compared to income tax expense of $37.0 million and $6.4 million for 2016 and 2015, respectively. The income tax benefit recorded in 2017 was mostly attributable to the tax benefit related to storm-related charges to the provision for loan and lease losses and the $13.2 million tax benefit recorded as a result of the change in tax status of certain subsidiaries from taxable corporations to limited liability companies that have elected to be treated as partnerships for income tax purposes in Puerto Rico. The increase in income tax expense for 2016, when compared to 2015, was mainly driven by higher taxable income, as the year 2015 was impacted by a pre-tax loss of $48.7 million on the bulk sale of assets. The effective tax rate for the year ended December 31, 2017 was (8%) compared to 28% and 23% for 2016 and 2015, respectively. As of December 31, 2017, the Corporation had a net deferred tax asset of $294.8 million (net of a valuation allowance of $191.2 million, including a valuation allowance of $150.7 million against the deferred tax assets of the Corporation's banking subsidiary, FirstBank). Refer to *Income Taxes* below for additional information.

- As of December 31, 2017, total assets were approximately $12.3 billion, an increase of $338.8 million from December 31, 2016. The increase primarily reflects a $416.7 million increase in cash and cash equivalents, largely driven by the deposit build-up experienced after the hurricanes. The funds from the deposit build-up are being maintained at the Federal Reserve Bank cash account pending better information about the volatility of these funds. This variance was partially offset by: (i) a $53.4 million decrease in total loans, before the allowance for loan and lease losses, primarily reflecting reductions of $293.3 million and $43.1 million in Puerto Rico and the Virgin Islands, respectively, including the sale of the PREPA credit line with a book value of $64 million at the time of sale, charge-offs of $30.8 million and cash collections of $10.2 million during 2017 on TDF commercial mortgage loans, the repayment of a $40.5 million commercial loan, the resolution of a $27.6 million non-performing commercial relationship in Puerto Rico, and a $74.9 million reduction in residential mortgage loans in Puerto Rico, partially offset by $283.0 million growth in the Florida region, primarily reflected in the commercial and residential loan portfolios; and (ii) a $26.2 million increase in the allowance for loan and lease losses driven by the establishment of the storm-related allowance amounting to $68.5 million as of December 31, 2017. Refer to *Financial Condition and Operating Data* below for additional information.

- As of December 31, 2017, total liabilities were $10.4 billion, an increase of $256.0 million, from December 31, 2016. The increase was mainly related to a $480.6 million increase in non-brokered deposits, reflecting increases of $363.9 million and $141.6 million in Puerto Rico and the Virgin Island regions, respectively, partially offset by a $24.8 million decrease in the Florida region. A significant portion of the increase was in noninterest-bearing demand deposits, which grew 24%, or $349.5 million, which, in part, reflects the effect of storm-related factors such as the payment deferral programs and disaster relief funds. In addition, FHLB advances increased by $45.0 million during 2017 reflecting increases in long-term FHLB advances as a source of funding for lending activities. These variances were partially offset by a $289.2 million decrease in brokered CDs. Refer to *Risk Management – Liquidity and Capital Adequacy* below for additional information about the Corporation’s funding sources.

- As of December 31, 2017, the Corporation’s stockholders’ equity was $1.9 billion, an increase of $82.9 million from December 31, 2016. The increase was mainly driven by the earnings generated in 2017, exclusive of the $12.2 million OTTI charge to earnings in 2017 and previously included as part of other comprehensive loss in total equity. The Corporation’s Total Capital, Common equity Tier 1 Capital, Tier 1 Capital and Leverage ratios calculated under the Basel III rules were 22.53%, 18.96%, 18.97%, and 14.03%, respectively, as of December 31, 2017, compared to Total Capital, Common equity Tier 1 Capital, Tier 1 Capital and Leverage ratios of 21.34%, 17.74%, 17.74%, and 13.70%, respectively, as of December 31, 2016. The Corporation’s tangible common equity ratio increased to 14.65% as of December 31, 2017, from 14.34% as of December 31, 2016. Refer to *Risk Management – Capital* below for additional information.

- Total loan production, including purchases, refinancings and draws from existing revolving and non-revolving commitments, was $2.9 billion for each of the years ended December 31, 2017 and 2016, excluding the utilization activity on outstanding credit cards. Similar levels were achieved despite the interruption and drop in business activity after the hurricanes as the declines observed in Puerto Rico and the Virgin Islands were almost entirely offset by increased volumes in the Florida region. Total loan production in Puerto Rico and the Virgin Islands regions decreased in 2017, as compared to 2016, by $205.9 million and $48.4 million, respectively, offset by a $244.8 million increase in the Florida region primarily reflected in the commercial segment.

• Total non-performing assets were $650.6 million as of December 31, 2017, a decrease of $83.9 million from December 31, 2016. The decrease was primarily attributable to the sale of the Corporation's participation in the PREPA credit line with a book value of $64 million at the time of sale, charge-offs of $30.8 million and cash collections of $10.2 million during 2017 on TDF commercial mortgage loans, the sale of non-performing bonds of the GDB and the Puerto Rico Public Buildings Authority with a book value at the time of sale of $23.0 million, the resolution of a $27.6 million non-performing commercial relationship in Puerto Rico, and a $7.3 million decrease in non-performing consumer loans. As part of the aforementioned commercial relationship resolution, the Corporation received a cash payment of $12.8 million, recorded charge-offs of $3.5 million, and acquired collateral amounting to $10.6 million transferred to the OREO portfolio.

These variances were partially offset by the inflow to non-performing status in the third quarter of two large commercial relationships in Puerto Rico totaling $34.2 million, the inflow in the fourth quarter of seven storm-affected commercial credits, each individually in excess of $1 million and totaling $25.5 million, and an increase of $17.4 million in non-performing residential mortgage loans. As mentioned above, interruptions in regular collection efforts and loss mitigation efforts relating to Hurricanes Irma and Maria as well as the direct effect of the hurricanes on certain commercial credits adversely affected the non-performing residential and commercial loan statistics in the latter part of 2017. Refer to *Risk Management - Non-accruing and Non-performing Assets* below for additional information.

• Adversely classified commercial and construction loans held for investment decreased by $15.2 million to $474.2 million, or 3%, from $489.4 million as of December 31, 2016, driven by the reduction in non-performing loans discussed in the above bullet.

Critical Accounting Policies and Practices

The accounting principles of the Corporation and the methods of applying these principles conform to GAAP. The Corporation's critical accounting policies relate to: 1) the allowance for loan and lease losses; 2) other-than-temporary impairments; 3) income taxes; 4) the classification and values of financial instruments; 5) income recognition on loans; 6) loans acquired; and 7) loans held for sale. These critical accounting policies involve judgments, estimates and assumptions made by management that affect the amounts recorded for assets, liabilities and contingent liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from estimates, if different assumptions or conditions prevail. Certain determinations inherently require greater reliance on the use of estimates, assumptions, and judgments and, as such, have a greater possibility of producing results that could be materially different than those originally reported.

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 Corporation does not maintain an allowance for held-for-sale loans or PCI loans that are performing in accordance with or better than expectations as of the date of acquisition, as the fair values of these loans already reflect a credit component. 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. The determination of the allowance for loan and lease losses requires significant estimates, including with respect to the timing and amounts of expected future cash flows on impaired loans, consideration of current economic conditions, and historical loss experience pertaining to the portfolios and pools of homogeneous loans, all of which may be susceptible to change.

The Corporation evaluates the need for changes to the allowance by portfolio loan segments and classes of loans within certain of those portfolio segments. The Corporation combines loans with similar credit risk characteristics into the following portfolio segments: commercial mortgage, construction, commercial and industrial, residential mortgage, and consumer loans. Classes are usually disaggregations of the portfolio segments. The classes within the residential mortgage segment are residential mortgages guaranteed by the U.S. government and other residential loans. The classes within the consumer portfolio are auto, finance lease, and other consumer loans. Other consumer loans mainly include unsecured personal loans, credit cards, home equity lines, lines of credits, and marine financing. The classes within the construction loan portfolio are land loans, construction of commercial projects, and construction of residential projects. The commercial mortgage and commercial and industrial segments are not further segmented into classes. The adequacy of the allowance for loan and lease losses is based on judgments related to the credit quality of each portfolio segment. These judgments consider ongoing evaluations of each portfolio segment, including such factors as the economic risks associated with each loan class, the financial condition of specific borrowers, the geography (Puerto Rico, Florida or the Virgin Islands), the level of delinquent loans, historical loss experience, the value of any collateral and, where applicable, the existence of any guarantees or other documented support. In addition to the general economic conditions and other factors described above, additional factors considered include the internal risk ratings assigned to loans. An internal risk rating is assigned to each commercial and construction loan at the time of approval and is subject to subsequent periodic review 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.

The allowance for loan and lease losses is increased through a provision for credit losses that is charged to earnings, based on the quarterly evaluation of the factors previously mentioned, and is reduced by charge-offs, net of recoveries.

The allowance for loan and lease losses consists of specific reserves based upon valuations of loans considered to be impaired, including loans modified in a TDR, and general reserves. A specific valuation allowance is established for individual impaired loans in the commercial mortgage, construction, and commercial and industrial portfolios and certain marine financings, residential mortgage loans, and home equity lines of credit, 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. The loans within the commercial mortgage, construction, commercial and industrial portfolios and marine financings with a principal balance of $1 million or more are individually evaluated for impairment. Also, certain residential mortgage loans and home equity lines of credit are individually evaluated for impairment purposes based on their delinquency and loan to value levels. When foreclosure of a collateral dependent loan is probable, the impairment measure is 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 generally updated annually thereafter according to the Corporation’s appraisal policy. In addition, appraisals and/or appraiser price opinions are also obtained for residential mortgage loans based on specific characteristics such as delinquency levels, age of the appraisal, and loan-to-value ratios. The excess of the recorded investment in a collateral dependent loan over the resulting fair value of the collateral is charged-off when deemed uncollectible.

For all other loans, which include small, homogeneous loans, such as auto loans, and the other classes in the consumer loan portfolio, residential mortgages and commercial and construction loans not considered impaired, the Corporation maintains a general valuation allowance established through a process that begins with estimates of incurred losses based upon various statistical analyses. The general reserve is primarily determined by applying loss factors according to the loan type and assigned risk category (pass, special mention, and substandard loans that are not considered to be impaired; all doubtful loans are considered impaired).

The Corporation uses a roll-rate methodology to estimate losses on its consumer loan portfolio based on delinquencies and considering credit bureau score bands. The Corporation tracks the historical portfolio performance to arrive at a weighted-average distribution in each subgroup of each delinquency bucket. Roll-to-loss rates (loss factors) are calculated by multiplying the roll rates from each subgroup within the delinquency buckets forward through loss. Once roll rates are calculated, the resulting loss factor is applied to the existing receivables in the applicable subgroups within the delinquency buckets and the end results are aggregated to arrive at the required allowance level. The Corporation's assessment also involves evaluating key qualitative and environmental factors, which include credit and macroeconomic indicators such as unemployment, bankruptcy trends, recent market transactions, and collateral values to account for current market conditions that are likely to cause estimated credit losses to differ from historical loss experience. The Corporation analyzes the expected delinquency migration to determine the future volume of delinquencies.

The cash flow analysis for each residential mortgage pool is performed at the individual loan level and then aggregated to the pool level in determining the overall expected loss ratio. The model applies risk-adjusted prepayment curves, default curves, and severity curves to each loan in the pool. For loan restructuring pools, the present value of expected future cash flows under the new terms, at the loan's effective interest rate, is taken into consideration. Additionally, estimates of default risk and prepayments related to loan restructurings are based on, among other things, the historical experience of these loans. Loss severity is affected by the expected house price scenario, which is based in part on recent house price trends. Default curves are used in the model to determine expected delinquency levels. The attributes that are most significant to the probability of default include present collection status (current, delinquent, in bankruptcy, in foreclosure stage), vintage, loan-to-values, and geography (Puerto Rico, Florida or the Virgin Islands).The estimates of the risk-adjusted timing of liquidations and associated costs are used in the model, and are risk-adjusted for the geographic area in which each property is located.

For commercial loans, historical charge-off rates are calculated by the Corporation on a quarterly basis by tracking cumulative charge-offs experienced over a two-year loss period on loans according to their internal risk rating (referred to as the "base rate" for the quarter). The allowance is calculated using the base rate average of the last 8 quarters. A qualitative factor adjustment is applied to the base rate average utilizing a resulting factor derived from a set of risk-based ratings and weights assigned to credit and economic indicators over a reasonable period applied to a developed expected range of historical losses. This factor may be stressed to reflect other elements not reflected in the historical data underlying the loss estimates, such as the prolonged uncertainty surrounding how the Puerto Rico government might restructure its debt and other unprecedented measures implemented by the Puerto Rico government to deal with its fiscal condition.

Storm-related Allowance for Loan and Lease Losses

During 2017, management determined a separate qualitative element of the allowance to represent the estimate of inherent losses associated with the effect of Hurricanes Maria and Irma on the Corporation’s loan portfolios in Puerto Rico and the Virgin Islands. This qualitative element of the allowance was determined based on the estimated effect that the storms could have on current employment levels (e.g., an unemployment rate that significantly increases from current levels in Puerto Rico based on statistics observed in the aftermath of similar natural disasters in the U.S. mainland like Hurricane Katrina), economic activity in the Corporation’s geographic regions, and the time it could take for the affected regions to return to a more normalized operating environment.

The Corporation’s credit risk modeling framework used to determine the storm-related qualitative estimate is similar to the one used for benchmarking purposes as part of the annual Dodd-Frank Act Stress Testing (“DFAST”) regulatory exercise. Models were developed following a regression modeling approach in which relationships between portfolio-level loss rates and key economic indicators were derived based on historical behavior. These models went through an extensive model specification and selection process that resulted in the use of certain variables, such as the unemployment rate and the Puerto Rico Economic Activity Index, which showed the highest predictive power of potential losses in our outstanding loan portfolio.

For large commercial and construction loan relationships, loan officers performed individual reviews of the effect of the storms on these borrowers’ sources of repayment. These large relationships, that represent 80% of the outstanding balance of the Corporation’s commercial and construction loan portfolio, were analyzed and divided into three storm-affected categories (i.e. Low, Medium and High). Clients categorized as Low had no effect, or relatively insignificant effect, as a result of the storms. Clients in the Medium category had demonstrated that they had sufficient liquidity to satisfy their obligations, but the complexity of the insurance claim process may affect their primary or secondary sources of repayment. Finally, clients categorized as High could potentially have problems with their primary or secondary sources of repayment as they have a higher degree of uncertainty with respect to the timing of the insurance claim resolution, and the full reestablishment of their businesses is highly dependent on the timely receipt of insurance proceeds. Reserve levels were then recognized for these particular loans based on this stratification. For loans in the Low category, no additional qualitative storm-related reserve was calculated. For loans in the Medium and High categories, the Corporation stressed the general reserve loss factors applicable to these loans to reflect higher default probabilities not reflected in the historical data.

This review also resulted in downgrades in the credit risk classification of certain loans and their reserves were determined following the methodology applicable to criticized and adversely classified loans, as appropriate.

For commercial and construction loans not individually reviewed, as well as residential and consumer loans, the estimated loss associated with the storms was determined following the above-described qualitative storm-related model with resulting loss factors applied to the overall performing balance of each portfolio.

As a result of the aforementioned analyses, the Corporation recorded a provision of $71.3 million in 2017 associated with the storms. As of December 31, 2017, the storm-related allowance was $68.5 million (net of a $2.8 million charge-off taken in the fourth quarter of 2017). Refer to *Provision for Loan and Lease Losses* below for additional information, including details about the storm-related allowance segregated by loans portfolio segments and geographic regions.

Charge-off of Uncollectible Loans - Net charge-offs consist of the unpaid principal balances of loans held for investment that the Corporation determines are uncollectible, net of recovered amounts. Charge-offs are recorded as a reduction to the allowance for loan and lease losses and subsequent recoveries of previously charged off amounts are credited to the allowance for loan and lease losses. Collateral dependent loans in the construction, commercial mortgage, and commercial and industrial loan portfolios are charged off to their net realizable value (fair value of collateral, less estimated costs to sell) when loans are considered to be uncollectible. Within the consumer loan portfolio, auto loans and finance leases are reserved once they are 120 days delinquent and are charged off to their estimated net realizable value when the collateral deficiency is deemed uncollectible (i.e., when foreclosure/repossession is probable) or when the loan is 365 days past due. Within the other consumer loan portfolios, closed-end loans are charged off when payments are 120 days in arrears, except small personal loans. Open-end (revolving credit) consumer loans, including credit card loans, and small personal loans are charged off when payments are 180 days in arrears. On a quarterly basis, residential mortgage loans that are 180 days delinquent and have an original loan-to-value ratio that is higher than 60% are reviewed and charged-off, as needed, to the fair value of the underlying collateral. Generally, all loans may be charged off or written down to the fair value of the collateral prior to the application of the policies described above if a loss-confirming event has occurred. Loss-confirming events include, but are not limited to, bankruptcy (unsecured), continued delinquency, or receipt of an asset valuation indicating a collateral deficiency when the asset is the sole source of repayment. The Corporation does not record charge-offs on PCI loans that are performing in accordance with or better than expectations as of the date of acquisition, as the fair value of these loans already reflects a credit component. The Corporation records charge-offs on PCI loans only if actual losses exceed estimated losses incorporated into the fair value recorded at acquisition and the amount is deemed uncollectible.

Other-than-temporary impairments ("OTTI")

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

The Corporation evaluates whether the impairment is other-than-temporary depending upon whether the portfolio consists of debt 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 debt 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, any adverse change to the credit conditions and liquidity of the issuer, taking into consideration the latest information available about the financial condition of the issuer, credit ratings, the failure of the issuer to make scheduled principal or interest payments, recent legislation and government actions affecting the issuer's industry, and actions taken by the issuer to deal with the economic climate. The Corporation also takes into consideration changes in the near-term prospects of the underlying collateral of a security, if any, such as changes in default rates, loss severity given default, and significant changes in prepayment assumptions and the level of cash flows generated from the underlying collateral, if any, supporting the principal and interest payments of the debt securities. OTTI must be 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, it must evaluate expected cash flows to be received and determine if a credit loss has occurred. An unrealized loss is generally deemed to be other-than-temporary and a credit loss is deemed to exist if the present value of the expected future cash flows is less than the amortized cost basis of the debt security. The credit loss component of an OTTI, if any, is recorded as net impairment losses on debt securities in the statements of income, while the remaining portion of the impairment loss is recognized in OCI, net of taxes, and included as a component of stockholders' equity provided the Corporation does not intend to sell the underlying debt security and it is more likely than not that the Corporation will not have to sell the debt security prior to recovery. 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 as long as the security is not placed in non-accrual status. Debt securities held by the Corporation at year-end primarily consisted of securities issued by U.S. government-sponsored entities, bonds issued by the Puerto Rico government, and private label MBS. Given the explicit and implicit guarantees provided by the U.S. Federal government, the Corporation believes the credit risk in securities issued by the U.S. government-sponsored entities is low. The Corporation's OTTI assessment was concentrated on Puerto Rico government debt securities and private label MBS. For further information, including methodology and assumptions used for the discounted cash flow analyses performed on these securities, refer to Note 6, *"Investment Securities,"* to the consolidated financial statements included in Item 8 of this form 10-K.

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 on, among other things, 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 and credit ratings, if applicable, 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 the book value in a reasonable time frame, it records an impairment by writing the security down to its 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 12 consecutive months or more. The Corporation's holding of equity securities on its available for sale portfolio amounted to $0.4 million.

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 tax 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 that are recognized as a reduction to the Corporation's effective tax rate in the year of resolution. Unfavorable settlement of any particular issue could increase the effective tax rate and may require the use of cash in the year of resolution.

Income tax expense includes Puerto Rico and USVI 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. and USVI income tax purposes and is generally subject to U.S. and USVI income tax only on its income from sources within the U.S. and USVI or income effectively connected with the conduct of a trade or business in those regions. Any such tax paid in the U.S. and USVI is also creditable against the Corporation's Puerto Rico tax liability, subject to certain conditions and limitations.

Under the Puerto Rico Internal Revenue Code of 2011, as amended (the "2011 PR Code"), the Corporation and its subsidiaries are treated as separate taxable entities and are not entitled to file consolidated tax returns and, thus, the Corporation is generally not able to utilize losses from one subsidiary to offset gains in another subsidiary. Accordingly, in order to obtain a tax benefit from a net operating loss ("NOL"), a particular subsidiary must be able to demonstrate sufficient taxable income within the applicable NOL carry-forward period. The 2011 PR Code allows entities organized as limited liability companies to perform an election to become a non-taxable "pass-through" entity and utilize losses to offset income from other "pass-through" entities, subject to certain limitations, with the remaining net income passing-through to its partner entities. The 2011 PR Code also provides a dividend received deduction of 100% on dividends received from "controlled" subsidiaries subject to taxation in Puerto Rico and 85% on dividends received from other taxable domestic corporations.

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 an International Banking Entity ("IBE") unit of the Bank, and through the Bank's subsidiary, FirstBank Overseas Corporation, whose interest income and gain on sales is exempt from Puerto Rico income taxation. The IBE and FirstBank Overseas Corporation were created under the International Banking Entity Act of Puerto Rico, which provides for total Puerto Rico tax exemption on net income derived by IBEs operating in Puerto Rico on the specific activities identified in the IBE Act. An IBE that operates as a unit of a bank pays income taxes at the corporate standard rate to the extent that the IBE's net income exceeds 20% of the bank's total net taxable income.

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 asset 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 the valuation allowance from period to period are included in the Corporation's tax provision in the period of change.

During 2017, management reassessed the need for a valuation allowance and concluded, based upon the assessment of all positive and negative evidence, that it is more likely than not that FirstBank will generate sufficient taxable income within the applicable NOL carry-forward periods to realize $294.7 million of its deferred tax assets. The positive evidence considered by management to assess on the adequacy of the valuation allowance as of December 31, 2017 included factors such as: FirstBank's three-year cumulative gain position; forecasts of future profitability under several potential scenarios that support the partial utilization of NOLs prior to their expiration between 2021 through 2024; and three consecutive years of taxable income. These factors demonstrate demand for FirstBank's products and services and improvements in credit quality measures that have resulted in reduced credit exposures, and have resulted in improvements in both sustainability of profitability and management's ability to forecast future losses. The negative evidence considered by management includes: consideration of the uncertainty surrounding the future economic conditions of the hurricane-affected areas, its probable effects on the loan portfolios' credit quality, the uncertainty related to the Puerto Rico government's financial condition, and the still elevated levels of non-performing assets.

The authoritative accounting guidance prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of income tax uncertainties with respect to positions taken or expected to be taken on income tax returns. Under this guidance, income tax benefits are recognized and measured based on a two-step analysis: 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 at 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 analysis and the tax benefit claimed on a tax return is referred to as an unrecognized tax benefit ("UTB"). As of December 31, 2017, the Corporation did not have UTBs recorded on its books.

Refer to Note 27, *"Income Taxes,"* to the consolidated financial statements for the year ended December 31, 2017 included in Item 8 of this Form 10-K, for further information related to Income Taxes.

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, if any, 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 OCI (a component of stockholders’ equity), and do not affect earnings until realized or are deemed to be other-than-temporarily impaired. New accounting guidance with respect to the accounting for equity securities effective beginning on January 1, 2018, requires the measurement of equity investments at fair value through net income, with certain exceptions, thus, eliminating eligibility for the current available-for-sale category. Investments in equity securities that do not have publicly or 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 assessment 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, the rates at which prepayments occur 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 mainly to manage liquidity needs and interest rate risks. A significant part of the Corporation’s total assets is reflected at fair value on the Corporation’s financial statements.

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

Investment securities available for sale

The fair value of investment securities available for sale was the market value based on quoted market prices (as is the case with equity securities, Treasury notes, and non-callable U.S. Agency debt securities), when available (Level 1), or, when available, market prices for identical or comparable assets (as is the case with MBS and callable U.S. agency debt) that are based on observable market parameters, including benchmark yields, reported trades, quotes from brokers or dealers, issuer spreads, bids, offers and reference data, including market research operations (Level 2). Observable prices in the market already consider the risk of nonperformance. If listed prices or quotes are not available, fair value is based upon discounted cash flow models that use unobservable inputs due to the limited market activity of the instrument, as is the case with certain private label mortgage-backed securities held by the Corporation (Level 3).

Private label MBS are collateralized by fixed-rate mortgages on single-family residential properties in the U.S.; the interest rate on the securities is variable, tied to 3-month LIBOR and limited to the weighted-average coupon of the underlying collateral. The market valuation represents the estimated net cash flows over the projected life of the pool of underlying assets applying a discount rate that reflects market observed floating spreads over LIBOR, with a widening spread based on a nonrated security. The market valuation is derived from a model that utilizes relevant assumptions such as the 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, and others) in combination with prepayment forecasts based on historical portfolio performance. 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, using an asset-level risk assessment method taking into account loan credit characteristics (loan-to-value, state jurisdiction, delinquency, property type and pricing behavior, and other factors) to provide an estimate of default and loss severity.

Derivative instruments

The fair value of most of the Corporation’s derivative instruments is based on observable market parameters and takes into consideration the credit risk component of paying counterparties, when appropriate. On interest rate caps, only the seller's credit risk is considered. The caps were valued using a discounted cash flow approach using the related LIBOR and swap rate for each cash flow.

A credit spread is considered for those derivative instruments that are not secured. The cumulative mark-to-market effect of credit risk in the valuation of derivative instruments in 2017, 2016 and 2015 was immaterial.

Income Recognition on Loans and Impaired Loans

Loans that the Corporation has the ability and intent to hold for the foreseeable future are classified as held for investment. The substantial majority of the Corporation’s loans are classified as held for investment. Loans are stated at the principal outstanding balance, net of unearned interest, cumulative charge-offs, 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 that approximates the interest method over the term of the loan as an adjustment to interest yield. Unearned interest on certain personal loans, auto loans and finance leases and discounts and premiums are recognized as income under a method that approximates the interest method. When a loan is paid-off or sold, any unamortized net deferred fee (cost) is credited (charged) to income. Credit card loans are reported at their outstanding unpaid principal balance plus uncollected billed interest and fees net of amounts deemed uncollectible. PCI loans are reported net of any remaining purchase accounting adjustments. See “Loans Acquired” below for the accounting policy for PCI loans.

Non-Performing and Past-Due Loans **-** Loans on which the recognition of interest income has been discontinued are designated as non-performing. Loans are classified as non-performing when they are 90 days past due for interest and principal, with the exception of residential mortgage loans guaranteed by the Federal Housing Administration (the “FHA”) or the Veterans Administration (the “VA”) and credit cards. It is the Corporation’s policy to report delinquent mortgage loans insured by the FHA or guaranteed by the VA as loans past due 90 days and still accruing as opposed to non-performing loans since the principal repayment is insured. However, the Corporation discontinues the recognition of income for FHA/VA loans when such loans are over 15 months delinquent. As permitted by regulatory guidance issued by the Federal Financial Institutions Examination Council (“FFIEC”), credit card loans are generally charged off in the period in which the account becomes 180 days past due. Credit card loans continue to accrue finance charges and fees until charged off at 180 days. Loans generally may be placed on non-performing status prior to when required by the policies described above when the full and timely collection of interest or principal becomes uncertain (generally based on an assessment of the borrower’s financial condition and the adequacy of collateral, if any). When a loan is placed on non-performing status, any accrued but uncollected interest income is reversed and charged against interest income and amortization of any net deferred fees is suspended. Interest income on non-performing loans is recognized only to the extent it is received in cash. However, when 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). Generally, the Corporation returns a loan to accrual status when all delinquent interest and principal becomes current under the terms of the loan agreement, or after a sustained period of repayment performance (6 months) and the loan is well secured and in the process of collection, and full repayment of the remaining contractual principal and interest is expected. PCI loans are not reported as non-performing as these loans were written down to fair value at the acquisition date and the accretable yield is recognized in interest income over the remaining life of the loans. Loans that are past due 30 days or more as to principal or interest are considered delinquent, with the exception of residential mortgage, commercial mortgage, and construction loans, which are considered past due when the borrower is in arrears on two or more monthly payments.

Impaired Loans **-** 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, or the loan has been modified in a TDR. Loans with insignificant delays or insignificant shortfalls in the amounts of payments expected to be collected are not considered to be impaired. The Corporation evaluates individually for impairment those loans in the construction, commercial mortgage, commercial and industrial, and marine financing portfolios with a principal balance of $1 million or more. Loans in the construction, commercial mortgage, and commercial and industrial portfolios that originally met the Corporation’s threshold for impairment evaluation but due to charge-offs or payments are currently below the $1 million threshold and are still 90 days past due, except TDR’s, are accounted for under the Corporation’s general reserve. Although the authoritative accounting guidance for a specific impairment of a loan excludes large groups of smaller balance homogeneous loans that are collectively evaluated for impairment (e.g., mortgage and consumer loans), it specifically requires that loan modifications considered TDRs be analyzed under its provisions. The Corporation also evaluates for impairment purposes certain residential mortgage loans and home equity lines of credit with high delinquency and loan to value levels. Held-for-sale loans are not reported as impaired, as these loans are recorded at the lower of cost or fair value.

The Corporation generally measures impairment and the related specific allowance for individually impaired loans based on the difference between the recorded investment of the loan and the present value of the loans’ expected future cash flows, discounted at the effective original interest rate of the loan at the time of modification, or the loan’s observable market price. If the loan is collateral dependent, the Corporation measures impairment based upon the fair value of the underlying collateral, instead of discounted cash flows, regardless of whether foreclosure is probable. Loans are identified as collateral dependent if the repayment is expected to be provided solely by the underlying collateral, through liquidation or operation of the collateral. When the fair value of the collateral is used to measure impairment on an impaired collateral-dependent loan and repayment or satisfaction of the loan is dependent on the sale of the collateral, the fair value of the collateral is adjusted to consider estimated costs to sell. If repayment is dependent only on the operation of the collateral, the fair value of the collateral is not adjusted for estimated costs to sell. If the fair value of the loan is less than the recorded investment, the Corporation recognizes impairment by either a direct write-down or establishing a specific allowance for the loan or by adjusting the specific allowance for the impaired loan. For an impaired loan that is collateral dependent, charge-offs are taken in the period in which the loan, or a portion of the loan, is deemed uncollectible, and any portion of the loan that is not charged off is adversely credit-risk rated at a level no worse than substandard.

A restructuring of a loan constitutes a TDR if the creditor, for economic or legal reasons related to the debtor’s financial difficulties, grants a concession to the debtor that it would not otherwise consider. TDR loans typically result from the Corporation’s loss mitigation activities and the modification of residential mortgage loans in accordance with guidelines similar to those of the U.S. government's Home Affordable Modification Program, and could include rate reductions to a rate that is below market on the loan, principal forgiveness, term extensions, payment forbearance, refinancing of any past-due amounts, including interest, escrow, and late charges and fees, and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of collateral. Residential mortgage loans for which a binding offer to restructure has been extended are also classified as TDR loans. PCI loans are not classified as TDR loans.

TDR loans are classified as either accrual or nonaccrual. Loans in accrual status may remain in accrual status when their contractual terms have been modified in a TDR if the loans had demonstrated performance prior to the restructuring and payment in full under the restructured terms is expected. Otherwise, a loan on nonaccrual status and restructured as a TDR will remain on nonaccrual status until the borrower demonstrates a sustained period of performance (generally six consecutive months of payments, inclusive of consecutive payments made prior to the modification), and there is evidence that such payments can and are likely to continue as agreed. Refer to Note 9, *"Loans Held for Investment,"* to the consolidated financial statements for the year ended December 31, 2017, included in Item 8 of this Form 10-K, for additional qualitative and quantitative information about TDR loans.

In connection with commercial loan restructurings, the decision to maintain a loan that has been restructured on accrual status is based on a current, well-documented credit evaluation of the borrower's financial condition and prospects for repayment under the modified terms. The credit evaluation reflects consideration of the borrower's future capacity to pay, which may include evaluation of cash flow projections, consideration of the adequacy of collateral to cover all principal and interest, and trends indicating improving profitability and collectability of receivables. This evaluation also includes an evaluation of the borrower's current willingness to pay, which may include a review of past payment history, an evaluation of the borrower's willingness to provide information on a timely basis, and consideration of offers from the borrower to provide additional collateral or guarantor support.

The evaluation of mortgage and consumer loans for restructurings includes an evaluation of the client's disposable income and credit report, the value of the property, the loan-to-value relationship, and certain other client-specific factors that have affected the borrower's ability to make timely principal and interest payments on the loan. In connection with residential and consumer restructurings, a nonperforming loan will be returned to accrual status when current as to principal and interest, under the revised terms, and upon sustained historical repayment performance.

The Corporation removes loans from TDR classification, consistent with authoritative guidance that allows for a TDR to be removed from this classification in years following the modification, only when the following two circumstances are met:

(i) The loan is in compliance with the terms of the restructuring agreement and, therefore, is not considered impaired under the revised terms; and

(ii) The loan yields a market interest rate at the time of the restructuring. In other words, the loan was restructured with an interest rate equal to or greater than what the Corporation would have been willing to accept at the time of the restructuring for a new loan with comparable risk.

If both of the conditions are met, the loan can be removed from the TDR classification in calendar years after the year in which the restructuring took place. However, the loan continues to be individually evaluated for impairment. Loans classified as TDRs, including loans in trial payment periods (trial modifications), are considered impaired loans.

With respect to the restructuring of a loan into two new loan notes, or loan splits, generally, Note A of a loan split is restructured under market terms, and Note B is fully charged off. If Note A is in compliance with the restructured terms in years following the restructuring, Note A will be removed from the TDR classification and will continue to be individually evaluated for impairment.

A loan that had previously been modified in a TDR and is subsequently refinanced under current underwriting standards at a market rate with no concessionary terms is accounted for as a new loan and is no longer reported as a TDR.

Interest income on impaired loans is recognized based on the Corporation's policy for recognizing interest on accrual and non-accrual loans.

Loans Acquired

All purchased loans are recorded at fair value at the date of acquisition. Loans acquired with evidence of credit deterioration since their origination and where it is probable at the date of acquisition that the Corporation will not collect all contractually required principal and interest payments are considered PCI loans. Evidence of credit quality deterioration as of the purchase date may include statistics such as past due and non-accrual status, credit scores, and revised loan terms. PCI loans have been aggregated into pools based on common risk characteristics. Each pool is accounted for as a single asset with a single composite interest rate and an aggregate expectation of cash flows. In accounting for PCI loans, the difference between contractually required payments and the cash flows expected to be collected at acquisition is referred to as the nonaccretable difference. The nonaccretable difference, which is neither accreted into income nor recorded on the consolidated statements of financial condition, reflects estimated future credit losses expected to be incurred over the life of the pool of loans. The excess of cash flows expected to be collected over the estimated fair value of PCI loans is referred to as the accretable yield. This amount is not recorded on the statements of financial condition, but is accreted into interest income over the remaining life of the pool of loans, using the effective-yield method.

Subsequent to acquisition, the Corporation continues to estimate cash flows expected to be collected over the life of the PCI loans using models that incorporate current key assumptions such as default rates, loss severity, and prepayment speeds. Decreases in expected cash flows will generally result in an impairment charge to the provision for loan and lease losses and the establishment of an allowance for loan and lease losses. Increases in expected cash flows will generally result in a reduction in any allowance for loan and lease losses established subsequent to acquisition and an increase in the accretable yield. The adjusted accretable yield is recognized in interest income over the remaining life of the pool of loans.

Resolutions of loans may include sales of loans to third parties, receipt of payments in settlement with the borrower, or foreclosure of the collateral. The Corporation's policy is to remove an individual loan from a pool at its relative carrying amount. The carrying amount is defined as the loan's current contractually required payments receivable less its remaining nonaccretable difference and accretable yield, but excluding any post-acquisition loan loss allowance. To determine the carrying value, the Corporation performs a pro-rata allocation of the pool's total remaining nonaccretable difference and accretable yield to an individual loan in proportion to the loan's current contractually required payments receivable compared to the pool's total contractually required payments receivable. This removal method assumes that the amount received from resolution approximates pool performance expectations. The remaining accretable yield balance is unaffected and any material change in the remaining effective yield caused by this removal method is addressed by the Corporation's quarterly cash flow evaluation process for each pool. Modified PCI loans are not removed from a pool even if those loans would otherwise be deemed TDRs.

Because the initial fair value of PCI loans recorded at acquisition includes an estimate of credit losses expected to be realized over the remaining lives of the loans, the Corporation separately tracks and reports PCI loans and excludes these loans from its delinquency and non-performing loan statistics.

For acquired loans that are not deemed impaired at acquisition, subsequent to acquisition, the Corporation recognizes the difference between the initial fair value at acquisition and the undiscounted expected cash flows in interest income over the period in which substantially all of the inherent losses associated with the non-PCI loans at the acquisition date are estimated to occur. Thus, such loans are accounted for consistently with other originated loans, potentially being classified as nonaccrual or impaired, as well as being classified under the Corporation's standard practice and procedures. In addition, these loans are considered in the determination of the allowance for loan losses.

Loans held for sale

Loans that the Corporation intends to sell or that the Corporation does not have the ability and intent to hold for the foreseeable future are classified as held-for-sale loans. Loans held for sale are stated at the lower of aggregate cost or fair value. Generally, the loans held-for-sale portfolio consists of conforming residential mortgage loans that the Corporation intends to sell to GNMA and government-sponsored entities ("GSEs"), such as FNMA and FHLMC. Generally, residential mortgage loans held for sale are valued on an aggregate portfolio basis and the value is primarily derived from quotations based on the mortgage-backed securities market. The amount by which cost exceeds market value in the aggregate portfolio of loans held for sale, if any, is accounted for as a valuation allowance with changes therein included in the determination of net income and reported as part of mortgage banking activities in the consolidated statements of income. Loan costs and fees are deferred at origination and are recognized in income at the time of sale. The fair value of commercial and construction loans held for sale is primarily derived from external appraisals with changes in the valuation allowance reported as part of other non-interest income in the consolidated statements of income.

In certain circumstances, the Corporation transfers loans from/to held for sale or held for investment based on a change in strategy. If such a change in holding strategy is made, significant adjustments to the loans' carrying values may be necessary. Reclassifications of loans held for sale to held for investment are made at fair value on the date of transfer. Any difference between the carrying value and the fair value of a reclassified loan is recorded as an adjustment to non-interest income. Meanwhile, reclassification of loans held for investment to held for sale are made at the lower of cost or fair value on the date of transfer and establish a new cost basis upon transfer. Write-downs of loans transferred from held for investment to held for sale are recorded as charge-offs at the time of transfer.

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 repricing and maturity mismatch of the Corporation's assets and liabilities. Net interest income for the year ended December 31, 2017 was $491.6 million, compared to $484.1 million and $502.3 million for 2016 and 2015, respectively. On a tax-equivalent basis and excluding the changes in the fair value of derivative instruments, net interest income for the year ended December 31, 2017 was $505.3 million compared to $497.4 million and $520.0 million for 2016 and 2015, respectively.

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 the volume of interest-related assets and liabilities have affected the Corporation's net interest income. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in volume (changes in volume multiplied by prior period rates), and (ii) changes in rate (changes in rate multiplied by prior period volumes). Rate-volume variances (changes in rate multiplied by changes in volume) have been allocated to the changes in volume and rate based upon their respective percentage of the combined totals.

The net interest income is computed on an adjusted tax-equivalent basis and excluding the change in the fair value of derivative instruments. For the definition and reconciliation of this non-GAAP financial measure, refer to the discussions below.

Part I

	Average volume			Interest income(1) / expense			Average rate(1)		
Year Ended December 31, (Dollars in thousands)	**2017**	**2016**	**2015**	**2017**	**2016**	**2015**	**2017**	**2016**	**2015**
Interest-earning assets:									
Money market and other short-term investments	$ 416,578	$ 667,838	$ 775,848	$ 4,614	$ 3,365	$ 2,148	1.11%	0.50%	0.28%
Government obligations (2)	687,076	746,890	636,734	17,918	20,849	20,560	2.61%	2.79%	3.23%
Mortgage-backed securities	1,278,968	1,357,518	1,489,423	42,476	38,072	44,909	3.32%	2.80%	3.02%
FHLB stock	40,458	31,449	26,522	2,105	1,454	1,075	5.20%	4.62%	4.05%
Other investments	2,702	1,963	777	8	8	-	0.30%	0.41%	0.00%
Total investments (3)	2,425,782	2,805,658	2,929,304	67,121	63,748	68,692	2.77%	2.27%	2.34%
Residential mortgage loans	3,260,715	3,302,519	3,272,464	174,524	180,051	181,400	5.35%	5.45%	5.54%
Construction loans	140,038	143,095	169,666	4,898	5,225	6,357	3.50%	3.65%	3.75%
Commercial and industrial and commercial mortgage loans	3,723,356	3,694,988	3,821,843	174,666	160,329	162,496	4.69%	4.34%	4.25%
	242,303	229,632	228,709	17,538	17,349	18,259	7.24%	7.56%	7.98%

Finance leases									
Consumer loans	1,480,265	1,526,475	1,670,245	166,107	171,858	186,120	11.22%	11.26%	11.14%
Total loans (4)(5)	8,846,677	8,896,709	9,162,927						