

OFG BANCORP
Form 10-K
March 15, 2016

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

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

For the Fiscal Year Ended December 31, 2015

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 No. 001-12647

OFG Bancorp

Incorporated in the Commonwealth of Puerto Rico

IRS Employer Identification No. 66-0538893

Principal Executive Offices:

254 Muñoz Rivera Avenue

San Juan, Puerto Rico 00918

Telephone Number: (787) 771-6800

Securities Registered Pursuant to Section 12(b) of the Act:

Common Stock (\$1.00 par value per share)

7.125% Noncumulative Monthly Income Preferred Stock, Series A (\$25.00 liquidation preference per share)

7.0% Noncumulative Monthly Income Preferred Stock, Series B (\$25.00 liquidation preference per share)

8.75% Noncumulative Convertible Perpetual Preferred Stock, Series C (\$1,000.00 liquidation preference per share)

7.125% Noncumulative Perpetual Preferred Stock, Series D (\$25.00 liquidation preference per share)

Securities Registered Pursuant to Section 12(g) of the Act: None

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

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of the common stock held by non-affiliates of OFG Bancorp (the "Company") was approximately \$473.4 million as of June 30, 2015 based upon 44,367,909 shares outstanding and the reported closing price of \$10.67 on the New York Stock Exchange on that date.

As of January 31, 2016, the Company had 43,867,909 shares of common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

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Portions of the Company's definitive proxy statement relating to the 2016 annual meeting of shareholders are incorporated herein by reference in response to Items 10 through 14 of Part III, except for certain information set forth herein under Item 12.

OFG Bancorp

FORM 10-K

For the Year Ended December 31, 2015

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FORWARD-LOOKING STATEMENTS

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

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

- a credit default or potential restructuring by the Commonwealth of Puerto Rico or any of its agencies, municipalities or instrumentalities;
- possible legislative, tax or regulatory changes;
- the rate of growth in the economy and employment levels, as well as general business and economic conditions;
- the relative strength or weakness of the consumer and commercial credit sectors and of the real estate market in Puerto Rico;
- competition in the financial services industry;
- the fiscal and monetary policies of the federal government and its agencies;
- changes in interest rates, as well as the magnitude of such changes;
- changes in federal bank regulatory and supervisory policies, including required levels of capital;
- the impact of the industry regulations on the Company’s businesses, business practices and cost of operations;
- the performance of the securities markets; and
- additional Federal Deposit Insurance Corporation (“FDIC”) assessments.

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

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

ITEM 1. *BUSINESS*

General

The Company is a publicly-owned financial holding company incorporated on June 14, 1996 under the laws of the Commonwealth of Puerto Rico, providing a full range of banking and financial services through its subsidiaries. The Company is subject to the provisions of the U.S. Bank Holding Company Act of 1956, as amended, (the “BHC Act”) and accordingly, subject to the supervision and regulation of the Board of Governors of the Federal Reserve System (the “Federal Reserve Board”).

The Company provides comprehensive banking and financial services to its clients through a complete range of banking and financial solutions, including commercial, consumer, auto, and mortgage lending; checking and savings accounts; financial planning, insurance, financial services, and investment brokerage; and corporate and individual trust and retirement services. The Company operates through three major business segments: Banking, Wealth Management, and Treasury, differentiating the Oriental brand through customer segmentation and innovative solutions, primarily in Puerto Rico. The Company provides these services through various subsidiaries including, a commercial bank, Oriental Bank, a securities broker-dealer, Oriental Financial Services Corp. (“Oriental Financial Services”), an insurance agency, Oriental Insurance, LLC (“Oriental Insurance”), previously known as Oriental Insurance Inc., and a retirement plan administrator, Oriental Pension Consultants, Inc. (“OPC”), previously known as Caribbean Pension Consultants, Inc. All of our subsidiaries are based in San Juan, Puerto Rico, except for OPC which is based in Boca Raton, Florida. The Company has 48 branches in Puerto Rico. The Company’s long-term goal is to strengthen its banking and financial services franchise by expanding its lending businesses, increasing the level of integration in the marketing and delivery of banking and financial services, maintaining effective asset-liability management, growing non-interest revenue from banking and financial services, and improving operating efficiencies.

The Company’s strategy involves:

- Strengthening its banking and financial services franchise by expanding its ability to attract deposits and build relationships with customers by refining the service delivery and providing innovative banking technologies for day-to-day customer transactions, and achieving sustainable levels of differentiation in the market;
- Focusing on greater growth in commercial, consumer and mortgage lending, trust and financial services and insurance products;
- Improving operating efficiencies, and continuing to maintain effective asset-liability management;
- Implementing a broad ranging effort to instill in employees and make customers aware of the Company’s determination to effectively serve and advise its customer base in a responsive and professional manner; and
- Matching its portfolio of investment securities with the related funding to achieve favorable spreads, and primarily investing in U.S. government-sponsored agency obligations.

Together with a highly experienced group of senior and mid-level executives and the benefits from the acquisitions of Eurobank Puerto Rico and the Puerto Rico operations of Banco Bilbao Vizcaya Argentaria, S.A. (“BBVA”), this strategy has resulted in sustained growth in the Company’s deposit-taking activities, commercial, consumer and mortgage lending and financial service activities, allowing the Company to distinguish itself in a highly competitive industry. The Company is not immune from general and local financial and economic conditions. Past experience is

not necessarily indicative of future performance, but given market uncertainties and on a reasonable time horizon of three to five years, this strategy is expected to maintain its steady progress towards the Company's long-term goal.

On December 18, 2012, the Company purchased from BBVA, all of the outstanding common stock of each of (i) BBVAPR Holding Corporation ("BBVAPR Holding"), the sole shareholder of Banco Bilbao Vizcaya Argentaria Puerto Rico ("BBVAPR Bank"), a Puerto Rico chartered commercial bank, and BBVA Seguros, Inc. ("BBVA Seguros"), a subsidiary offering insurance services, and (ii) BBVA Securities of Puerto Rico, Inc. ("BBVA Securities"), a registered broker-dealer. This transaction is referred to as the "BBVAPR Acquisition" and BBVAPR Holding, BBVAPR Bank, BBVA Seguros and BBVA Securities are collectively referred to as the "BBVAPR Companies" or "BBVAPR."

The Company's principal funding sources are branch deposits, securities sold under agreements to repurchase, Federal Home Loan Bank ("FHLB") advances, Federal Reserve Bank ("FRB") advances, wholesale deposits, and subordinated capital notes. Through its branch network, Oriental Bank offers personal non-interest and interest-bearing checking accounts, savings accounts, certificates of deposit, individual retirement accounts ("IRAs") and commercial non-interest bearing checking accounts. The FDIC insures Oriental Bank's deposit accounts up to applicable limits. Management makes retail deposit pricing decisions periodically, adjusting the rates paid on retail deposits in response to general market conditions and local competition. Pricing decisions take into account the rates being offered by other local banks, the London Interbank Offered Rate ("LIBOR"), and mainland U.S. market interest rates.

Segment Disclosure

The Company has three reportable segments: Banking, Wealth Management, and Treasury. Management established the reportable segments based on the internal reporting used to evaluate performance and to assess where to allocate resources. Other factors such as the Company's organizational structure, nature of products, distribution channels and economic characteristics of the products were also considered in the determination of the reportable segments. The Company measures the performance of these reportable segments based on pre-established annual goals involving different financial parameters such as net income, interest rate spread, loan production, and fees generated.

For detailed information regarding the performance of the Company's operating segments, please refer to Note 26 in the Company's accompanying consolidated financial statements.

Banking Activities

Oriental Bank (the "Bank"), the Company's main subsidiary, is a full-service Puerto Rico commercial bank with its main office located in San Juan, Puerto Rico. The Bank has 48 branches throughout Puerto Rico and was incorporated in October 1964 as a federal mutual savings and loan association. It became a federal mutual savings bank in July 1983 and converted to a federal stock savings bank in April 1987. Its conversion from a federally-chartered savings bank to a commercial bank chartered under the banking law of the Commonwealth of Puerto Rico, on June 30, 1994, allowed the Bank to more effectively pursue opportunities in its market and obtain more flexibility in its businesses. As a Puerto Rico-chartered commercial bank, it is subject to examination by the FDIC and the Office of the Commissioner of Financial Institutions of Puerto Rico (the "OCFI"). The Bank offers banking services such as commercial, consumer, and mortgage lending, savings and time deposit products, financial planning, and corporate and individual trust services, and capitalizes on its retail banking network to provide commercial and mortgage lending products to its clients. The Bank operates two international banking entities ("IBE") pursuant to the International Banking Center Regulatory Act of Puerto Rico, as amended (the "IBE Act"), one is a unit operating within the Bank, named Oriental Overseas (the "IBE Unit"), and the other is a wholly-owned subsidiary of the Bank, named Oriental International Bank, Inc. (the "IBE Subsidiary"). The IBE Unit and IBE Subsidiary offer the Bank certain Puerto Rico tax advantages, and their services are limited under Puerto Rico law to persons and assets/liabilities located outside of Puerto Rico.

Banking activities include the Bank's branches and mortgage banking activities with traditional retail banking products such as deposits, commercial loans, consumer loans and mortgage loans. The Bank's significant lending activities are with consumers located in Puerto Rico. The Bank's lending transactions include a diversified number of industries and activities, all of which are encompassed within four main categories: commercial, consumer, mortgage and auto.

The Company's mortgage banking activities are conducted through a division of the Bank. The mortgage banking activities include the origination of mortgage loans for the Bank's own portfolio, and the sale of loans directly into the secondary market or the securitization of conforming loans into mortgage-backed securities. The Bank originates

Federal Housing Administration (“FHA”) insured mortgages, Veterans Administration (“VA”) guaranteed mortgages, and Rural Housing Service (“RHS”) guaranteed loans that are primarily securitized for issuance of Government National Mortgage Association (“GNMA”) mortgage-backed securities which can be resold to individual or institutional investors in the secondary market. Conventional loans that meet the underwriting requirements for sale or exchange under standard Federal National Mortgage Association (the “FNMA”) or the Federal Home Loan Mortgage Corporation (the “FHLMC”) programs are referred to as conforming mortgage loans and are also securitized for issuance of FNMA or FHLMC mortgage-backed securities. The Bank is an approved seller of FNMA, as well as FHLMC, mortgage loans for issuance of FNMA and FHLMC mortgage-backed securities. The Bank is also an approved issuer of GNMA mortgage-backed securities. The Company outsources the servicing of the GNMA, FNMA and FHLMC pools that it issues, and its residential mortgage loan portfolio.

Loan Underwriting

Auto loans: The Company provides financing for the purchase of new or used motor vehicles. These loans are granted mainly through dealers authorized and approved by the auto credit department committee of the Company. The auto credit department has the specialized structure and resources to provide the service required for this product according to market demands and trends. The auto loan credit policy establishes specific guidance and parameters for the underwriting and origination processes. Underwriting procedures, lending limits, interest rate approval, insurance coverage, and automobile brand restrictions are some parameters and internal controls implemented to ensure the quality and profitability of the auto loan portfolio. The credit scoring system is a fundamental part of the decision process.

Consumer loans: Consumer loans include personal loans, credit cards, lines of credit and other loans made by banks to individual borrowers. All loan originations must be underwritten in accordance with the Company's underwriting criteria, and include an assessment of each borrower's personal financial condition, including verification of income, assets, FICO score, and credit reports.

Residential mortgage loans: All loan originations, regardless of whether originated through the Company's retail banking network or purchased from third parties, must be underwritten in accordance with the Company's underwriting criteria, including loan-to-value ratios, borrower income qualifications, debt ratios and credit history, investor requirements, and title insurance and property appraisal requirements. The Company's mortgage underwriting standards comply with the relevant guidelines set forth by the Department of Housing and Urban Development ("HUD"), VA, FNMA, FHLMC, federal and Puerto Rico banking regulatory authorities, as applicable. The Company's underwriting personnel, while operating within the Company's loan offices, make underwriting decisions independent of the Company's mortgage loan origination personnel.

Commercial loans: Commercial loans include lines of credit and term facilities to finance business operations and to provide working capital for specific purposes, such as to finance the purchase of assets, equipment or inventory. Since a borrower's cash flow from operations is generally the primary source of repayment, the Company's analysis of the credit risk focuses heavily on the borrower's debt-repayment capacity. Commercial term loans generally have terms from one to five years, may be collateralized by the asset being acquired, real estate, or other available assets, and bear interest rates that float with the prime rate, LIBOR or another established index, or are fixed for the term of the loan. Lines of credit are extended to businesses based on an analysis of the financial strength and integrity of the borrowers and are generally secured primarily by real estate, accounts receivables or inventory, and have a maturity of one year or less. Such lines of credit bear an interest rate that floats with a base rate, the prime rate, LIBOR, or another established index.

Sale of Loans and Securitization Activities

The Company may engage in the sale or securitization of a portion of the residential mortgage loans that it originates and purchases and utilizes various channels to sell its mortgage products. The Company is an approved issuer of GNMA-guaranteed mortgage-backed securities which involves the packaging of FHA loans, RHS loans or VA loans into pools of mortgage-backed securities for sale primarily to securities broker-dealers and other institutional investors. The Company can also act as issuer in the case of conforming conventional loans in order to group them

into pools of FNMA or FHLMC-issued mortgage-backed securities which the Company then sells to securities broker-dealers. The issuance of mortgage-backed securities provides the Company with flexibility in selling the mortgage loans that it originates or purchases and also provides income by increasing the value and marketability of such loans. In the case of conforming conventional loans, the Company also has the option to sell such loans through the FNMA and FHLMC cash-window programs.

Wealth Management Activities

Wealth management activities are generated by such businesses as securities brokerage, trust services, retirement planning, insurance, pension administration, and other financial services.

Oriental Financial Services is a Puerto Rico corporation and the Company's subsidiary engaged in securities brokerage activities in accordance with the Company's strategy of providing fully integrated financial solutions to the Company's clients. Oriental Financial Services, member of FINRA and the Securities Investor Protection Corporation, is a registered securities broker-dealer pursuant to Section 15(b) of the Securities Exchange Act of 1934. The broker-dealer does not carry customer accounts and is, accordingly, exempt from the Customer Protection Rule (SEC Rule 15c3-3) pursuant to subsection (k)(2)(ii) of such rule. It clears securities transactions through Pershing LLC, a clearing agent that carries the accounts of its customers on a "fully disclosed" basis.

Oriental Financial Services offers securities brokerage services covering various investment alternatives such as tax-advantaged fixed income securities, mutual funds, stocks, and bonds to retail and institutional clients. It also offers separately-managed accounts and mutual fund asset allocation programs sponsored by unaffiliated professional asset managers. These services are designed to meet each client's specific needs and preferences, including transaction-based pricing and asset-based fee pricing.

Oriental Financial Services has managed and participated in public offerings and private placements of debt and equity securities in Puerto Rico and has engaged in municipal securities business with the Commonwealth of Puerto Rico and its instrumentalities, municipalities, and public corporations. Investment banking revenue from such activities includes gains, losses, and fees, net of syndicate expenses, arising from securities offerings in which it acts as an underwriter or agent. Investment banking revenue also includes fees earned from providing merger-and-acquisition and financial restructuring advisory services.

Oriental Insurance is a Puerto Rico limited liability company and the Company's subsidiary engaged in insurance agency services. It was established by the Company to take advantage of the cross-marketing opportunities provided by financial modernization legislation. Oriental Insurance currently earns commissions by acting as a licensed insurance agent in connection with the issuance of insurance policies by unaffiliated insurance companies and continues to cross market its services to the Company's existing customer base.

OPC, a Florida corporation, is the Company's subsidiary engaged in the administration of retirement plans in the U.S., Puerto Rico, and the Caribbean.

Treasury Activities

Treasury activities encompass all of the Company's treasury-related functions. The Company's investment portfolio consists of mortgage-backed securities, obligations of U.S. government-sponsored agencies, Puerto Rico government and agency obligations and money market instruments. Agency mortgage-backed securities, the largest component, consist principally of pools of residential mortgage loans that are made to consumers and then resold in the form of pass-through certificates in the secondary market, the payment of interest and principal of which is guaranteed by GNMA, FNMA or FHLMC.

Market Area and Competition

The main geographic business and service area of the Company is in Puerto Rico, where the banking market is highly competitive. Puerto Rico banks are subject to the same federal laws, regulations and supervision that apply to similar institutions in the United States of America. The Company also competes with brokerage firms with retail operations, credit unions, savings and loan cooperatives, small loan companies, insurance agencies, and mortgage banks in Puerto Rico. The Company encounters intense competition in attracting and retaining deposits and in its consumer and commercial lending activities. Management believes that the Company has been able to compete effectively for deposits and loans by offering a variety of transaction account products and loans with competitive terms, by emphasizing the quality of its service, by pricing its products at competitive interest rates, by offering convenient branch locations, and by offering financial planning and financial services at most of its branch locations. The phase-out consolidation of three failed Puerto Rico banks in 2010 and the failure of another Puerto Rico bank in 2015 has created an environment for more rational loan and deposit pricing. The Company's ability to originate loans depends primarily on the services that it provides to its borrowers, in making prompt credit decisions, and on the rates and fees that it charges.

Regulation and Supervision

General

The Company is a financial holding company subject to supervision and regulation by the Federal Reserve Board under the BHC Act, as amended by the Gramm-Leach-Bliley Act and the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). The qualification requirements and the process for a bank holding company that elects to be treated as a financial holding company requires that a bank holding company and all of the subsidiary banks controlled by it at the time of election must be and remain at all times “well capitalized” and “well managed.”

The Company elected to be treated as a financial holding company as permitted by the Gramm-Leach-Bliley Act. Under the Gramm-Leach-Bliley Act, if the Company fails to meet the requirements for being a financial holding company and is unable to correct such deficiencies within certain prescribed time periods, the Federal Reserve Board could require the Company to divest control of its depository institution subsidiary or alternatively cease conducting activities that are not permissible for bank holding companies that are not financial holding companies.

Financial holding companies may engage, directly or indirectly, in any activity that is determined to be (i) financial in nature or incidental to such financial activity, or (ii) complementary to a financial activity provided it does not pose a substantial risk to the safety and soundness of depository institutions or the financial system generally. The Gramm-Leach-Bliley 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, investment or economic advisory services; (d) securitization of assets; (e) securities underwriting and dealing; (f) existing bank holding company domestic activities; (g) existing bank holding company foreign activities; and (h) merchant banking activities. A financial holding company may generally commence any activity, or acquire any company, that is financial in nature without prior approval of the Federal Reserve Board. As provided by the Dodd-Frank Act, a financial holding company may not acquire a company, without prior Federal Reserve Board approval, in a transaction in which the total consolidated assets to be acquired by the financial holding company exceed \$10 billion.

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

The Company is required to file with the Federal Reserve Board and the SEC periodic reports and other information concerning its own business operations and those of its subsidiaries. In addition, Federal Reserve Board approval must also be obtained before a bank holding company acquires all or substantially all of the assets of another bank or merges or consolidates with another bank holding company. The Federal Reserve Board also has the authority to issue cease and desist orders against bank holding companies and their non-bank subsidiaries.

The Bank is regulated by various agencies in the United States and the Commonwealth of Puerto Rico. Its main regulators are the OCFI and the FDIC. The Bank is subject to extensive regulation and examination by the OCFI and the FDIC, and is subject to the Federal Reserve Board’s regulation of transactions between the Bank and its affiliates. The federal and Puerto Rico laws and regulations which are applicable to the Bank regulate, among other things, the scope of its business, its investments, its reserves against deposits, the timing of the availability of deposited funds, and the nature and amount of and collateral for certain loans. In addition to the impact of such 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 control inflation in the economy.

The Company’s mortgage banking business is subject to the rules and regulations of FHA, VA, RHS, FNMA, FHLMC, HUD and GNMA with respect to the origination, processing and selling of mortgage loans and the sale of mortgage-backed securities. Those rules and regulations, among other things, prohibit discrimination and establish underwriting guidelines which include provisions for inspections and appraisal reports, require credit reports on prospective borrowers and fix maximum loan amounts, and, with respect to VA loans, fix maximum interest rates. Mortgage origination activities are subject to, among others, the Equal Credit Opportunity Act, the Truth-in-Lending Act, the Real Estate Settlement Procedures Act and the regulations promulgated thereunder which, among other things, prohibit discrimination and require the disclosure of certain basic information to mortgagors concerning credit terms and settlement costs. The Company is also subject to regulation by the OCFI with respect to, among other things, licensing requirements and maximum origination fees on certain types of mortgage loan products.

The Company and its subsidiaries are subject to the rules and regulations of certain other regulatory agencies. Oriental Financial Services, as a registered broker-dealer, is subject to the supervision, examination and regulation of FINRA, the SEC, and the OCFI in matters relating to the conduct of its securities business, including record keeping and reporting requirements, supervision and licensing of employees, and obligations to customers.

Oriental Insurance is subject to the supervision, examination and regulation of the Office of the Commissioner of Insurance of Puerto Rico in matters relating to insurance sales, including but not limited to, licensing of employees, sales practices, charging of commissions and reporting requirements.

Dodd-Frank Wall Street Reform and Consumer Protection Act

The Dodd-Frank Act implements a variety of far-reaching changes and has been described as the most sweeping reform of the financial services industry since the 1930's. It has a broad impact on the financial services industry, including significant regulatory and compliance changes, such as: (i) enhanced resolution authority of troubled and failing banks and their holding companies; (ii) enhanced lending limits strengthening the existing limits on a depository institution's credit exposure to one borrower; (iii) increased capital and liquidity requirements; (iv) increased regulatory examination fees; (v) changes to assessments to be paid to the FDIC for federal deposit insurance; (vi) prohibiting bank holding companies, such as the Company, from including in regulatory Tier 1 capital future issuances of trust preferred securities or other hybrid debt and equity securities; and (vii) numerous other provisions designed to improve supervision and oversight of, and strengthening safety and soundness for, the financial services sector.

Additionally, the Dodd-Frank Act establishes a new framework for systemic risk oversight within the financial system to be distributed among new and existing federal regulatory agencies, including the Financial Stability Oversight Council, the Federal Reserve Board, the Office of the Comptroller of the Currency and the FDIC. Further, the Dodd-Frank Act addresses many corporate governance and executive compensation matters that affect most U.S. publicly traded companies, including the Company. A few provisions of the Dodd-Frank Act became effective immediately, while various provisions have become effective in stages. Many of the requirements called for in the Dodd-Frank Act have been implemented over time and most are subject to implementing regulations.

The Dodd-Frank Act also created a new consumer financial services regulator, the Bureau of Consumer Financial Protection (the “CFPB”), which assumed most of the consumer financial services regulatory responsibilities previously exercised by federal banking regulators and other agencies. The CFPB’s primary functions include the supervision of “covered persons” (broadly defined to include any person offering or providing a consumer financial product or service and any affiliated service provider) for compliance with federal consumer financial laws. It has primary authority to enforce the federal consumer financial laws, as well as exclusive authority to require reports and conduct examinations for compliance with such laws, in the case of any insured depository institution with total assets of more than \$10 billion and any affiliate thereof. The CFPB also has broad powers to prescribe rules applicable to a covered person or service provider identifying as unlawful, unfair, deceptive, or abusive acts or practices in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service.

Holding Company Structure

The Bank is subject to restrictions under federal laws that limit the transfer of funds to its affiliates (including the Company), whether in the form of loans, other extensions of credit, investments or asset purchases, among others. Such transfers are limited to 10% of the transferring institution’s capital stock and surplus with respect to any affiliate (including the Company), and, with respect to all affiliates, to an aggregate of 20% of the transferring institution’s capital stock and surplus. Furthermore, such loans and extensions of credit are required to be secured in specified amounts, carried out on an arm’s length basis, and consistent with safe and sound banking practices.

Under the Dodd-Frank Act, a bank holding company, such as the Company, must serve as a source of financial strength for any subsidiary depository institution. The term “source of financial strength” is defined as the ability of a company to provide financial assistance to its insured depository institution subsidiaries in the event of financial distress at such subsidiaries. This support may be required at times when, absent such requirement, 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 are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary bank. The Bank is currently the only depository institution subsidiary of the Company.

Since the Company is a financial holding company, its right to participate in the assets of any subsidiary upon the latter’s liquidation or reorganization will be subject to the prior claims of the subsidiary’s creditors (including depositors in the case of the Bank) except to the extent that the Company is a creditor with recognized claims against the subsidiary.

Dividend Restrictions

The principal source of funds for the Company is the dividends from the Bank. The ability of the Bank to pay dividends on its common stock is restricted by the Puerto Rico Banking Act of 1933, as amended (the “Banking Act”),

the Federal Deposit Insurance Act, as amended (the “FDIA”), and the FDIC regulations. In general terms, the Banking Act provides that when the expenditures of a bank are greater than its receipts, the excess of expenditures over receipts shall be charged against the undistributed profits of the bank and the balance, if any, shall be charged against the required reserve fund of the bank. If there is no sufficient reserve fund to cover such balance in whole or in part, the outstanding amount shall be charged against the bank’s capital account. The Banking Act 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 a bank.

The payment of dividends by the Bank may also be affected by other regulatory requirements and policies, such as maintenance of adequate capital. If, in the opinion of the regulatory authority, a depository institution under its jurisdiction is engaged in, or is about to engage in, an unsafe or unsound practice (that, depending on the financial condition of the depository institution, could include the payment of dividends), such authority may require, after notice and hearing, that such depository institution cease and desist from such practice. The Federal Reserve Board has a policy statement that provides that an insured bank or bank holding company should not maintain its existing rate of cash dividends on common stock unless (i) the organization's net income available to common shareholders over the past year has been sufficient to fully fund the dividends and (ii) the prospective rate of earnings retention appears consistent with the organization's capital needs, asset quality, and overall financial condition. In addition, all insured depository institutions are subject to the capital-based limitations required by the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA").

Federal Home Loan Bank System

The FHLB system, of which the Bank is a member, consists of 12 regional FHLBs governed and regulated by the Federal Housing Finance Agency. The FHLB serves as a credit facility for member institutions within their assigned regions. They are funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB system. They make loans (i.e., advances) to members in accordance with policies and procedures established by the FHLB and the boards of directors of each regional FHLB.

As a system member, the Bank is entitled to borrow from the FHLB of New York (the "FHLB-NY") and is required to invest in FHLB membership and activity-based stock. The Bank must purchase membership stock equal to the greater of \$1,000 or 0.15% of certain mortgage-related assets held by the Bank. The Bank is also required to purchase activity-based stock equal to 4.50% of outstanding advances to the Bank by the FHLB. The Bank is in compliance with the membership and activity-based stock ownership requirements described above. All loans, advances and other extensions of credit made by the FHLB to the Bank are secured by a portion of the Bank's mortgage loan portfolio, certain other investments, and the capital stock of the FHLB held by the Bank. The Bank is required to maintain a minimum amount of qualifying collateral with a fair value of at least 110% of the outstanding advances.

Prompt Corrective Action Regulations

Pursuant to the Dodd-Frank Act, federal banking agencies have adopted capital rules that became effective January 1, 2014 for advanced approaches banking organizations (i.e., those with consolidated assets greater than \$250 billion or consolidated on-balance sheet foreign exposures of at least \$10 billion) and January 1, 2015 for all other covered organizations (subject to certain phase-in periods through January 1, 2019) and that will replace their general risk-based capital rules, advanced approaches rule, market risk rule, and leverage rules.

The new capital rules provide certain changes to the prompt corrective action regulations adopted by the agencies under Section 38 of the FDIA, as amended by FDICIA. These regulations are designed to place restrictions on U.S. insured depository institutions if their capital levels begin to show signs of weakness. The five capital categories established by the agencies under their prompt corrective action framework are: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized".

The new capital rules expand such categories by introducing a common equity tier 1 capital requirement for all depository institutions, revising the minimum risk-based capital ratios and, beginning in 2018, the proposed supplementary leverage requirement for advanced approaches banking organizations. The common equity tier 1 capital ratio is a new minimum requirement designed to ensure that banking organizations hold sufficient high-quality regulatory capital that is available to absorb losses on a going-concern basis. Under the new rules, an insured depository institution is:

(i) “well capitalized,” if it has a total risk-based capital ratio of 10% or more, a tier 1 risk-based capital ratio of 8% or more, a common equity tier 1 capital ratio of 6.5% or more, and a tier 1 leverage capital ratio of 5% or more, and is not subject to any written capital order or directive;

(ii) “adequately capitalized,” if it has a total risk-based capital ratio of 8% or more, a tier 1 risk-based capital ratio of 6% or more, a common equity tier 1 capital ratio of 4.5% or more, and a tier 1 leverage capital ratio of 4% or more;

(iii) “undercapitalized,” if it has a total risk-based capital ratio that is less than 8%, a tier 1 risk-based ratio that is less than 6%, a common equity tier 1 capital ratio that is less than 4.5%, or a tier 1 leverage capital ratio that is less than 4%;

(iv) “significantly undercapitalized,” if it has a total risk-based capital ratio that is less than 6%, a tier 1 risk-based capital ratio that is less than 4%, a common equity tier 1 capital ratio that is less than 3%, or a tier 1 leverage capital ratio that is less than 3%; and

(v) “critically undercapitalized,” if it has a ratio of tangible equity (defined as tier 1 capital plus non-tier 1 perpetual preferred stock) to total assets that is equal to or less than 2%.

The new capital rules also include a policy statement by the agencies that all banking organizations should maintain capital commensurate with their risk profiles, which may entail holding capital significantly above the minimum requirements. They also provide a reservation of authority permitting examiners to require that such organizations hold additional regulatory capital.

FDICIA generally prohibits a depository institution from making any capital distribution (including payment of a dividend) or paying any management fees to its holding company if the depository institution would thereafter be undercapitalized. Undercapitalized depository institutions are subject to restrictions on borrowing from the Federal Reserve System. In addition, undercapitalized depository institutions are subject to growth limitations and are required to submit capital restoration plans. A depository institution’s holding company must guarantee the capital plan, up to an amount equal to the lesser of 5% of the depository institution’s assets at the time it becomes undercapitalized or the amount of the capital deficiency when the institution fails to comply with the plan. The federal banking agencies may not accept a capital plan without determining, among other things, that the plan is based on realistic assumptions and is likely to succeed in restoring the depository institution’s capital. Significantly undercapitalized depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets, and cessation of receipt of deposits from correspondent banks. Critically undercapitalized depository institutions are subject to the appointment of a receiver or conservator.

FDIC Insurance Assessments

The Bank is subject to FDIC deposit insurance assessments. The Federal Deposit Insurance Reform Act of 2005 (the “Reform Act”) merged the Bank Insurance Fund (“BIF”) and the Savings Association Insurance Fund (“SAIF”) into a single Deposit Insurance Fund, and increased the maximum amount of the insurance coverage for certain retirement accounts, and possible “inflation adjustments” in the maximum amount of coverage available with respect to other insured accounts. In addition, it granted a one-time initial assessment credit (of approximately \$4.7 billion) to recognize institutions’ past contributions to the fund. As a result of the merger of the BIF and the SAIF, all insured institutions are subject to the same assessment rate schedule.

The Dodd-Frank Act contains several important deposit insurance reforms, including the following: (i) the maximum deposit insurance amount was permanently increased to \$250,000; (ii) the deposit insurance assessment is now based on the insured depository institution’s average consolidated assets minus its average tangible equity, rather than on its deposit base; (iii) the minimum reserve ratio for the Deposit Insurance Fund was raised from 1.15% to 1.35% of estimated insured deposits by September 30, 2020; (iv) the FDIC is required to “offset the effect” of increased assessments on insured depository institutions with total consolidated assets of less than \$10 billion; (v) the FDIC is no longer required to pay dividends if the Deposit Insurance Fund’s reserve ratio is greater than the minimum ratio; and (vi) the FDIC temporarily insured the full amount of qualifying “noninterest-bearing transaction accounts” until December 31, 2012. As defined in the Dodd-Frank Act, a “noninterest-bearing transaction account” is a deposit or

account maintained at a depository institution with respect to which interest is neither accrued nor paid, on which the depositor or account holder is permitted to make withdrawals by negotiable or transferrable instrument, payment orders of withdrawals, telephone or other electronic media transfers, or other similar items for the purpose of making payments or transfers to third parties or others, and on which the insured depository institution does not reserve the right to require advance notice of an intended withdrawal.

The FDIC amended its regulations under the FDIA, as amended by the Dodd-Frank Act, to modify the definition of a depository institution's insurance assessment base; to revise the deposit insurance assessment rate schedules in light of the new assessment base and altered adjustments; to implement the dividend provisions of the Dodd-Frank Act; and to revise the large insured depository institution assessment system to better differentiate for risk and better take into account losses from large institution failures that the FDIC may incur. Since the new assessment base under the Dodd-Frank Act is larger than the current assessment base, the new assessment rates adopted by the FDIC are lower than the former rates.

Brokered Deposits

FDIC regulations adopted under the FDIA govern the receipt of brokered deposits by banks. Well capitalized institutions are not subject to limitations on brokered deposits, while adequately capitalized institutions are able to accept, renew or rollover brokered deposits only with a waiver from the FDIC and subject to certain restrictions on the interest paid on such deposits. Undercapitalized institutions are not permitted to accept brokered deposits. As of December 31, 2015, the Bank is a well capitalized institution and is therefore not subject to these limitations on brokered deposits.

Regulatory Capital Requirements

Under the Dodd-Frank Act, federal banking regulators are required to establish minimum leverage and risk-based capital requirements, on a consolidated basis, for insured institutions, depository institution holding companies, and non-bank financial companies supervised by the Federal Reserve Board. The minimum leverage and risk-based capital requirements are to be determined based on the minimum ratios established for insured depository institutions under prompt corrective action regulations. In effect, such provision of the Dodd-Frank Act, which is commonly known as the Collins Amendment, applies to bank holding companies the same leverage and risk-based capital requirements that apply to insured depository institutions. Because the capital requirements must be the same for insured depository institutions and their holding companies, the Collins Amendment generally excludes certain debt or equity instruments, such as cumulative perpetual preferred stock and trust preferred securities, from Tier 1 Capital, subject to a three-year phase-out from Tier 1 qualification for such instruments issued before May 19, 2010, with the phase-out commencing on January 1, 2014 for advanced approaches banking organizations and January 1, 2015 for other bank holding companies with consolidated assets of \$15 billion or more as of December 31, 2009. However, such instruments issued before May 19, 2010 by a bank holding company, such as the Company, with a total consolidated assets of less than \$15 billion as of December 31, 2009, are not affected by the Collins Amendments, are “grandfathered” under the new capital rules, and may continue to be included in tier 1 Capital as a restricted core capital element.

The new capital rules adopted by the federal banking agencies revise the agencies’ risk-based and leverage capital requirements for banking organizations, and consolidate three separate notices of proposed rulemaking that the OCC, Federal Reserve Board and FDIC published in the Federal Register on August 30, 2012, with selected changes. In particular, and consistent with the framework of the Basel Committee on Banking Supervision in “Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems,” the new capital rules include a minimum ratio of common equity tier 1 capital to risk-weighted assets of 4.5% and a common equity tier 1 capital conservation buffer of 2.5% of risk-weighted assets that apply to all banking organizations. The rules also raise the minimum ratio of tier 1 capital to risk-weighted assets from 4% to 6% and include a minimum leverage ratio of 4% for all banking organizations. In addition, for the largest, most internationally active banking organizations, the rules include a new minimum supplementary leverage ratio that takes into account off-balance sheet exposures. The rules incorporate these new requirements into the agencies’ prompt corrective action framework. In addition, the rules establish limits on a banking organization’s capital distributions and certain discretionary bonus payments if the banking organization does not hold a specified amount of common equity tier 1 capital in addition to the amount necessary to meet its minimum risk-based capital requirements. Further, the rules amend the methodologies for determining risk-weighted assets for all banking organizations; introduce disclosure requirements that would apply to top-tier banking organizations domiciled in the United States with \$50 billion or more in total assets; and adopt changes to the agencies’ regulatory capital requirements that meet the requirements of Section 171 and Section 939A of the Dodd-Frank Act. These rules also codify the agencies’ current capital rules, which have previously resided in various appendices to their respective regulations, into a harmonized integrated regulatory framework.

Failure to meet the capital guidelines could subject an institution to a variety of enforcement actions including the termination of deposit insurance by the FDIC and to certain restrictions on its business. At December 31, 2015, the Company was in compliance with all applicable capital requirements. For more information, please refer to the accompanying consolidated financial statements.

Safety and Soundness Standards

Section 39 of the FDIA, as amended by FDICIA, requires each federal banking agency to prescribe for all insured depository institutions standards relating to internal control, information systems, and internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, fees and benefits, and such other operational and managerial standards as the agency deems appropriate. In addition, each federal banking agency also is required to adopt for all insured depository institutions standards relating to asset quality, earnings and stock valuation that the agency determines to be appropriate. Finally, each federal banking agency is required to prescribe standards for the employment contracts and other compensation arrangements of executive officers, employees, directors and principal stockholders of insured depository institutions that would prohibit compensation, benefits and other arrangements that are excessive or that could lead to a material financial loss for the institution. If an institution fails to meet any of the standards described above, it will be required to submit to the appropriate federal banking agency a

plan specifying the steps that will be taken to cure the deficiency. If the institution fails to submit an acceptable plan or fails to implement the plan, the appropriate federal banking agency will require the institution to correct the deficiency and, until it is corrected, may impose other restrictions on the institution, including any of the restrictions applicable under the prompt corrective action provisions of FDICIA.

The FDIC and the other federal banking agencies have adopted Interagency Guidelines Establishing Standards for Safety and Soundness that, among other things, set forth standards relating to internal controls, information systems and internal audit systems, loan documentation, credit, underwriting, interest rate exposure, asset growth and employee compensation.

Activities and Investments of Insured State-Chartered Banks

Section 24 of the FDIA, as amended by FDICIA, generally limits the activities and equity investments of FDIC-insured, state-chartered banks to those that are permissible for national banks. Under FDIC regulations of equity investments, an insured state bank generally may not directly or indirectly acquire or retain any equity investment of a type, or in an amount, that is not permissible for a national bank. An insured state bank, such as the Bank, is not prohibited from, among other things, (i) acquiring or retaining a majority interest in a subsidiary engaged in permissible activities, (ii) investing as a limited partner in a partnership, or as a non-controlling interest holder of a limited liability company, the sole purpose of which is direct or indirect investment in the acquisition, rehabilitation or new construction of a qualified housing project, provided that such investments may not exceed 2% of the bank's total assets, (iii) acquiring up to 10% of the voting stock of a company that solely provides or reinsures directors', trustees' and officers' liability insurance coverage or bankers' blanket bond group insurance coverage for insured depository institutions, and (iv) acquiring or retaining the voting stock of an insured depository institution if certain requirements are met, including that it is owned exclusively by other banks. Under the FDIC regulations governing the activities and investments of insured state banks which further implemented Section 24 of the FDIA, as amended by FDICIA, an insured state-chartered bank may not, directly, or indirectly through a subsidiary, engage as "principal" in any activity that is not permissible for a national bank unless the FDIC has determined that such activities would pose no risk to the Deposit Insurance Fund and the bank is in compliance with applicable regulatory capital requirements.

Transactions with Affiliates and Related Parties

Transactions between the Bank and any of its affiliates are governed by sections 23A and 23B of the Federal Reserve Act. These sections are important statutory provisions designed to protect a depository institution from transferring to its affiliates the subsidy arising from the institution's access to the Federal safety net. An affiliate of a bank is any company or entity that controls, is controlled by, or is under common control with the bank, including investment funds for which the bank or any of its affiliates is an investment advisor. Generally, sections 23A and 23B (i) limit the extent to which a bank or its subsidiaries may engage in "covered transactions" with any one affiliate to an amount equal to 10% of the bank's capital stock and surplus, and limit such transactions with all affiliates to an amount equal to 20% of such capital stock and surplus, and (ii) require that all such transactions be on terms that are consistent with safe and sound banking practices. The term "covered transactions" includes the making of loans, purchase of or investment in securities issued by the affiliate, purchase of assets, acceptance of securities issued by the affiliate as collateral for a loan or extension of credit, issuance of guarantees and other similar types of transactions. The Dodd-Frank Act expanded the scope of transactions treated as "covered transactions" to include credit exposure to an affiliate on derivatives transactions, credit exposure resulting from a securities borrowing or lending transaction, or derivative transaction, and acceptances of affiliate-issued debt obligations as collateral for a loan or extension of credit. Most loans by a bank to any of its affiliates must be secured by collateral in amounts ranging from 100% to 130% of the loan amount, depending on the nature of the collateral. In addition, any covered transaction by a bank with an affiliate and any sale of assets or provision of services to an affiliate must be on terms that are substantially the same, or at least as favorable to the bank, as those prevailing at the time for comparable transactions with nonaffiliated

companies. Regulation W of the Federal Reserve Board comprehensively implements sections 23A and 23B. The regulation unified and updated staff interpretations issued over the years prior to its adoption, incorporated several interpretative proposals (such as to clarify when transactions with an unrelated third party will be attributed to an affiliate), and addressed issues arising as a result of the expanded scope of non-banking activities engaged in by banks and bank holding companies and authorized for financial holding companies under the Gramm-Leach-Bliley Act.

Sections 22(g) and 22(h) of the Federal Reserve Act place restrictions on loans by a bank to executive officers, directors, and principal shareholders. Regulation O of the Federal Reserve Board implements these provisions. Under Section 22(h) and Regulation O, loans to a director, an executive officer and to greater-than-10% shareholders of a bank and certain of their related interests (“insiders”), and insiders of its affiliates, may not exceed, together with all other outstanding loans to such person and its related interests, the bank’s single borrower limit (generally equal to 15% of the institution’s unimpaired capital and surplus). Section 22(h) and Regulation O also require that loans to insiders and to insiders of affiliates be made on terms substantially the same as offered in comparable transactions to other persons, unless the loans are made pursuant to a benefit or compensation program that (i) is widely available to employees of

the bank and (ii) does not give preference to insiders over other employees of the bank. Section 22(h) and Regulation O also require prior board of directors' approval for certain loans, and the aggregate amount of extensions of credit by a bank to all insiders cannot exceed the institution's unimpaired capital and surplus. Furthermore, Section 22(g) and Regulation O place additional restrictions on loans to executive officers.

Community Reinvestment Act

Under the Community Reinvestment Act ("CRA"), a financial institution has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. The CRA requires federal examiners, in connection with the examination of a financial institution, to assess the institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by such institution. The CRA also requires all institutions to make public disclosure of their CRA ratings. The Company has a Compliance Department that oversees the planning of products and services offered to the community, especially those aimed to serve low and moderate income communities.

USA Patriot Act

Under Title III of the USA Patriot Act, also known as the International Money Laundering Abatement and Anti-Terrorism Financing Act of 2001, all financial institutions, including the Company, Oriental Financial Services, and the Bank, are required in general to 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.

The U.S. Treasury Department (the "US Treasury") has issued a number of regulations implementing the USA Patriot Act that apply certain of its requirements to financial institutions. The regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing.

Failure of a financial institution to comply with the USA Patriot Act's requirements could have serious legal consequences for the institution. The Company and its subsidiaries, including the Bank, have adopted policies, procedures and controls to address compliance with the USA Patriot Act under existing regulations, and will continue to revise and update their policies, procedures and controls to reflect changes required by the USA Patriot Act and the US Treasury's regulations.

Privacy Policies

Under the Gramm-Leach-Bliley Act, all financial institutions are required to adopt privacy policies, restrict the sharing of nonpublic customer data with nonaffiliated parties at the customer's request, and establish procedures and practices to protect customer data from unauthorized access. The Company and its subsidiaries have established policies and procedures to assure the Company's compliance with all privacy provisions of the Gramm-Leach-Bliley Act.

Sarbanes-Oxley Act

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

The Company has included in this annual report on Form 10-K management’s assessment regarding the effectiveness of the Company’s internal control over financial reporting. The internal control report includes a statement of management’s responsibility for establishing and maintaining adequate internal control over financial reporting for the Company; management’s assessment as to the effectiveness of the Company’s internal control over financial reporting based on management’s evaluation as of year-end; and the framework used by management as criteria for evaluating the effectiveness of the Company’s internal control over financial reporting. As of December 31, 2015, the Company’s management concluded that its internal control over financial reporting was effective.

Puerto Rico Banking Act

As a Puerto Rico-chartered commercial bank, the Bank is subject to regulation and supervision by the OCFI under the Banking Act, which contains provisions governing the incorporation and organization of the Bank, rights and responsibilities of directors, officers and stockholders, as well as the corporate powers, savings, lending, capital and investment requirements and other aspects of the Bank and its affairs. In addition, the OCFI is given extensive rulemaking power and administrative discretion under the Banking Act. The OCFI generally examines the Bank at least once every year.

The Banking Act requires that a minimum of 10% of the Bank's net income for the year be transferred to a reserve fund until such fund (legal surplus) equals the total paid-in capital on common and preferred stock. At December 31, 2015 and 2014, legal surplus amounted to \$70.4 million. The amount transferred to the legal surplus account is not available for the payment of dividends to shareholders.

The Banking Act also provides that when the expenditures of a bank are greater than the receipts, the excess of the former over the latter must be charged against the undistributed profits of the bank, and the balance, if any, must be charged against the reserve fund. If there is no reserve fund sufficient to cover such balance in whole or in part, the outstanding amount must be charged against the capital account and no dividend may be declared until said capital has been restored to its original amount and the reserve fund to 20% of the original capital.

The Banking Act further requires every bank to maintain a legal reserve which cannot be less than 20% of its demand liabilities, except government deposits (federal, commonwealth and municipal), which are secured by actual collateral.

The Banking Act also requires change of control filings. When any person or entity will own, directly or indirectly, upon consummation of a transfer, 5% or more of the outstanding voting capital stock of a bank, the acquiring parties must inform the OCFI of the details not less than 60 days prior to the date said transfer is to be consummated. The transfer will require the approval of the OCFI if it results in a change of control of the bank. Under the Banking Act, a change of control is presumed if an acquirer who did not own more than 5% of the voting capital stock before the transfer exceeds such percentage after the transfer.

The Banking Act permits Puerto Rico commercial banks to make loans to any one person, firm, partnership or corporation, up to an aggregate amount of 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 OCFI may determine from time to time. If such loans are secured by collateral worth at least 25% more than the amount of the loan, the aggregate maximum amount will include 33.33% of 50% of the bank's retained earnings. Such restrictions under the Banking Act on the amount of loans to a single borrower do not apply to loans: (i) to the government of the United States or the government of the Commonwealth of Puerto Rico, or any of their respective agencies, instrumentalities or municipalities, or (ii) that are wholly secured by bonds, securities and other evidence of indebtedness of the government of the United States or of the Commonwealth of Puerto Rico or by bonds, not in default, of municipalities or instrumentalities of the Commonwealth of Puerto Rico.

The Puerto Rico Finance Board is composed of the Commissioner of Financial Institutions of Puerto Rico; the Presidents of the Government Development Bank for Puerto Rico, the Economic Development Bank for Puerto Rico and the Planning Board; the Puerto Rico Secretaries of Commerce and Economic Development, Treasury and Consumer Affairs; the Commissioner of Insurance; and the President of the Public Corporation for Insurance and Supervision of Puerto Rico Credit Unions. It has the authority to regulate the maximum interest rates and finance charges that may be charged on loans to individuals and unincorporated businesses in the Commonwealth. The current

regulations of the Puerto Rico Finance Board provide that the applicable interest rate on loans to individuals and unincorporated businesses is to be determined by free competition. The Puerto Rico Finance Board also has the authority to regulate maximum finance charges on retail installment sales contracts and for credit card purchases. There is presently no maximum rate for retail installment sales contracts and for credit card purchases.

Puerto Rico Internal Revenue Code

On July 2014, the Governor signed into law Act No. 77-2014, known as “Ley de Ajustes al Sistema Contributivo” (Act of Adjustments to the Tax System). The main purpose of this legislation is to increase government collections in order to alleviate the structural budget deficit. Its most relevant provisions, as applicable to the Company, and effective for transactions held after June 30, 2014, are as follows: (1) the capital tax rate was increased from 15% to 20% and (2) for an asset to be considered long term capital asset, the holding period must be over a year, which before was defined with a holding period of over six months.

On May 29, 2015 the Governor signed Act No. 72 of 2015. The most relevant provisions of the Act No. 72, as applicable to the Company, for taxable years beginning after December 31, 2014, are as follows: (1) establishes a new definition of “large taxpayers,” which require them to file their tax return following a special procedure established by the Secretary of the Treasury, (2) net operating losses carried forward may be deducted up to 70% of the alternative minimum net income for purposes of computing the alternative minimum tax, and (3) net operating losses carried forward may be deducted up to 80% of the net income for purposes of computing the regular corporate income tax.

Other Code amendments applicable during 2015 are the increase of the Sales and Use Tax (SUT) from 7% to 11.5% beginning July 1st, 2015 and a special SUT to business to business transactions of 4%, beginning October 1st, 2015. These were implemented as a transitional phase to the enacted Value Added Tax (VAT) of 10.5%, which will be in place on April 1st, 2016, along with a Municipal SUT of 1% on certain taxable items.

International Banking Center Regulatory Act of Puerto Rico

The business and operations of the Bank’s IBE Unit and IBE Subsidiary are subject to supervision and regulation by the OCFI. Under the IBE Act, no sale, encumbrance, assignment, merger, exchange or transfer of shares, interest or participation in the capital of an IBE may be initiated without the prior approval of the OCFI if by such transaction a person would acquire, directly or indirectly, control of 10% or more of any class of stock, interest or participation in the capital of the IBE. The IBE Act and the regulations issued thereunder by the OCFI (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/liabilities located outside of Puerto Rico. The IBE Act provides further that every IBE must have not less than \$300 thousand of unencumbered assets or acceptable financial guarantees.

Pursuant to the IBE Act and the IBE Regulations, the Bank’s IBE Unit and IBE Subsidiary have to maintain books and records of all their transactions in the ordinary course of business. They are also required to submit quarterly and annual reports of their financial condition and results of operations to the OCFI, including annual audited financial statements.

The IBE Act empowers the OCFI to revoke or suspend, after notice and hearing, a license issued thereunder if, among other things, the IBE fails to comply with the IBE Act, the IBE Regulations or the terms of its license, or if the OCFI 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 IBE Act was superseded by a new law that, among other things, prohibits new license applications to organize and operate an IBE. Any such newly organized entity (now called an “international financial entity”) must be licensed under the new law, and such entity (as opposed to existing IBEs organized under the IBE Act, including the Bank’s IBE Unit and IBE Subsidiary, which are “grandfathered”) will generally be subject to a 4% Puerto Rico income tax rate.

Volcker Rule

The so-called “Volcker Rule” adopted by the federal banking regulatory agencies under Section 619 of the Dodd-Frank Act generally prohibits insured depository institutions and their affiliates from (i) engaging in short-term proprietary trading of securities, derivatives, commodities futures and options on these instruments for their own account; and (ii) owning, sponsoring or having certain relationships with hedge funds or private equity funds. However, it exempts certain activities, including market making, underwriting, hedging, trading in government and municipal obligations, and organizing and offering a hedge fund or private equity fund, among others. A banking entity that engages in any such covered activity (i.e., proprietary trading or investment activities in hedge funds or private equity funds) is generally required to establish an internal compliance program reasonably designed to ensure and monitor compliance with the Volcker Rule.

Employees

At December 31, 2015, the Company had 1,466 employees. None of its employees is represented by a collective bargaining group. The Company considers its employee relations to be good.

Internet Access to Reports

The Company’s annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any and all amendments to such reports, filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, are available free of charge on or through the “Investor Relations” link of the Company’s internet website at www.orientalbank.com, as soon as reasonably practicable after the Company electronically files such material with, or furnishes it to, the SEC.

The Company's corporate governance principles and guidelines, code of business conduct and ethics, and the charters of its audit committee, compensation committee, risk and compliance committee, and corporate governance and nominating committee are available free of charge on the Company's website at www.orientalbank.com in the investor relations section under the corporate governance link. The Company's code of business conduct and ethics applies to its directors, officers, employees and agents, including its principal executive, financial and accounting officers.

ITEM 1A. RISK FACTORS

In addition to other information set forth in this report, you should carefully consider the following risk factors, as updated by other filings the Company makes with the SEC under the Securities Exchange Act of 1934. Additional risks and uncertainties not presently known to us at this time or that the Company currently deems immaterial may also adversely affect the Company's business, financial condition or results of operations.

Most of our business is conducted in Puerto Rico, which in recent years has been experiencing a deep economic recession, a downturn in the real estate market, and a government fiscal and liquidity crisis.

Our loan and deposit activities are directly affected by economic conditions within Puerto Rico. Because a significant portion of our credit risk exposure on our loan portfolio, which is the largest component of our interest-earning assets, is concentrated in Puerto Rico, our profitability and financial condition may be adversely affected by an extended economic recession, adverse political, fiscal or economic developments in Puerto Rico, or the effects of a natural disaster, all of which could result in a reduction in loan originations, an increase in non-performing assets, an increase in foreclosure losses on mortgage loans, and a reduction in the value of our loans and loan servicing portfolio.

The Puerto Rico economy has been in a recession since 2006 and the Commonwealth government currently faces a severe fiscal and liquidity crisis as a result of many years of significant budget deficits, among other factors, which have adversely affected its ability to obtain financing at reasonable interest rates, if at all. Puerto Rico also faces high unemployment, unprecedented population decline, and high levels of government debt and pension obligations. A further deterioration in local economic conditions or in the financial condition of an industry on which the local market depends could adversely affect factors such as unemployment rates and real estate vacancy and values. This could result in, among other things, a reduction of creditworthy borrowers seeking loans, an increase in loan delinquencies, defaults and foreclosures, an increase in classified and non-accrual loans, a decrease in the value of collateral for or loans, and a decrease in core deposits. Any of these factors could materially impact our business.

For a discussion of the impact of the economy on our loan portfolios, see “—A prolonged economic downturn or recession or a continuing decline in the real estate market would likely result in an increase in delinquencies, defaults and foreclosures and in a reduction in loan origination activity, which would adversely affect our financial results.”

We are exposed to credit and concentration risk in connection with our loans to certain public corporations, instrumentalities and municipalities of Puerto Rico, and a credit default on their debt obligations could adversely affect the value of such loans and our financial condition.

Although the economy of Puerto Rico is closely related to the economy of the rest of the United States, the Commonwealth and its instrumentalities face a number of severe economic and fiscal challenges that, either individually or in the aggregate, could adversely affect the Commonwealth's ability to pay debt-service on its obligations when due. The three main credit rating agencies have downgraded all debt obligations of the Puerto Rico government to categories that are well below investment grade and a credit or payment default by at least two of the Commonwealth's public instrumentalities has occurred and additional defaults are generally expected. The downgrades are based mostly on concerns about Puerto Rico's economic recession, liquidity availability, sizable debt-obligations, high unemployment, shrinking population, unreliable forecasts for financial information, and the Puerto Rico government's lack of financial flexibility and limited capacity to borrow in the capital markets, which increase the Commonwealth's risk of default. Securities that are below investment grade present greater risks and are less liquid than investment-grade securities.

The Commonwealth government has unveiled a fiscal restructuring plan that, among other findings, provides that paying debt service on Puerto Rico's government obligations in the face of significant financing gaps could severely impair its ability to provide essential services to the residents of Puerto Rico. In this regard, it has proposed to seek a consensual restructuring of its outstanding debt and other tax-supported obligations. If the government is unable to restructure its debts and/or negotiate upcoming maturities and liquidity sources continue scarce, the government may have to declare a debt-service moratorium, default on its debt obligations, eliminate government agencies, cut essential programs or services, and take other emergency or extraordinary actions. Any further deterioration of economic or fiscal conditions in Puerto Rico could adversely affect the value of our loans to the government of Puerto Rico and the value of our investment portfolio of Puerto Rico government bonds.

At December 31, 2015, we had approximately \$415 million of credit facilities granted to the Puerto Rico government, including its instrumentalities, public corporations and municipalities, all of which was outstanding as of such date. A substantial portion of our

credit exposure to the government of Puerto Rico consists of collateralized loans or obligations that have a specific source of income or revenues identified for their repayment. Some of these obligations consist of senior and subordinated loans to public corporations that obtain revenues from rates charged for services or products, such as the Puerto Rico Electric Power Authority (“PREPA”). Public corporations have varying degrees of independence from the central government and many have received appropriations or are due other payments from it.

Oriental Bank is part of a four bank syndicate providing a \$550 million revolving line of credit to finance the purchase of fuel for PREPA’s day-to-day power generation activities. Our participation in the line of credit has an unpaid principal balance of \$190.3 million as of December 31, 2015. As part of the bank syndicate, the Bank entered into a forbearance agreement with PREPA, which was extended several times until the execution of a Restructuring Support Agreement on November 5, 2015 with PREPA and certain other creditors. The Restructuring Support Agreement provides for the restructuring of the fuel line of credit subject to the accomplishment of several milestones, including some milestones that depend on the actions of third parties to the agreement, such as the negotiation of agreements with other creditors and legislative action. The Company has classified the credit facility to PREPA as substandard and on non-accrual status. The Company conducted an impairment analysis considering the probability of collection of principal and interest, which included a financial model to project the future liquidity status of PREPA under various scenarios and its capacity to service its financial obligations, and concluded that PREPA had sufficient cash flows for the repayment of the line of credit. Despite the Company’s analysis showing PREPA’s capacity to repay the line of credit, the Company placed its participation in non-accrual during the first quarter of 2015 and recorded a \$53.3 million provision for loan and lease losses during 2015. Since April 1, 2015, interest payments have been applied to principal.

In June 2014, Puerto Rico enacted the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (the “Recovery Act”), which established procedures for the adjustment of debts of certain public corporations owned by the Commonwealth, which, as Puerto Rico governmental instrumentalities, are not currently eligible for federal bankruptcy relief under any chapter of the U.S. Bankruptcy Code. The Recovery Act states in its preamble that it further promotes the government’s public policy of no longer providing financial support to such public corporations, such as, for example, the PREPA, and promoting their economic independence. In February 2015, the United States District Court for the District of Puerto Rico held that the Recovery Act is preempted by the U.S. Bankruptcy Code and is therefore void pursuant to the Supremacy Clause of the United States Constitution. It also permanently enjoined the Commonwealth from enforcing the Recovery Act. The District Court’s decision was upheld on appeal by the United States Circuit Court of Appeals for the First Circuit. However, on December 4, 2015, the United States Supreme Court granted the Commonwealth’s petition for writ of certiorari to review the District Court’s decision. Oral arguments before the United States Supreme Court are scheduled for March 22, 2016. In addition, there are ongoing initiatives in Congress to make Chapter 9 of the U.S. Bankruptcy Code applicable to Puerto Rico and/or otherwise provide an orderly debt restructuring regime for the Commonwealth. In summary, the Commonwealth’s current ability to restructure the debts of some of its public corporations, such as PREPA, remains uncertain, and a broad disorderly restructuring with multiple creditor lawsuits and other legal actions

is possible.

PREPA’s enabling act provides for local receivership upon request to any Puerto Rico court of competent jurisdiction in the event of a default in debt-service payments or other obligations in connection with PREPA’s bonds. The

receiver so appointed would be empowered, directly or through its agents and attorneys, to take possession of the undertakings, income and revenues pledged to the payment of the bonds in default; to have, hold, use, operate, manage and control the same; and to exercise all of PREPA's rights and powers with respect to such undertakings. However, any such receiver would not have the power to sell, assign, mortgage or otherwise dispose of PREPA's assets, and its powers would be limited to the operation and maintenance of such undertakings and the collection and application of the income and revenues therefrom. These provisions have not been tested in the courts, and it is not clear if and how they would apply in connection with other debts and obligations of PREPA upon an event of default.

The PREPA Revitalization Act was recently signed into law by the Governor of Puerto Rico. It provides for a major debt restructuring of PREPA's outstanding debt and sets forth a legal framework for PREPA to execute on the agreements reached with its creditors. Among other things, it (i) enhances PREPA's governance processes; (ii) adjusts PREPA's practices for hiring and managing personnel; (iii) changes PREPA's processes for collecting outstanding bills from public and private entities; (iv) improves transparency of PREPA's billing practices; (v) implements a competitive bidding process for soliciting third party investment in PREPA's infrastructure; (vi) allows for the refinancing of existing PREPA bonds through a securitization that would reduce PREPA's indebtedness and cost of borrowing; and (vii) sets forth a process for the Energy Commission to address PREPA's proposal for a new rate structure that consistent with its recovery plan.

If our Commonwealth public debtors are unable to pay their obligations to us as they become due, or under certain other circumstances, we may be required to adversely classify such loans and provision for losses in connection therewith. Such provision may significantly impact our financial condition and our regulatory capital ratios.

Our decisions regarding credit risk and the allowance for loan and lease losses may materially and adversely affect our business and results of operations.

Making loans is an essential element of our business, and there is a risk that the loans will not be repaid. This default risk is affected by a number of factors, including:

- the duration of the loan;
- credit risks of a particular borrower;
- changes in economic or industry conditions; and
- in the case of a collateralized loan, risks resulting from uncertainties about the future value of the collateral.

Our customers might not repay their loans according to the original terms, and the collateral securing the payment of those loans might be insufficient to pay any remaining loan balance. Hence, we may experience significant loan losses, which could have a materially adverse effect on our operating results. We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. In determining the amount of the allowance for loan losses, we rely on loan quality reviews, past loss experience, and an evaluation of economic conditions, among other factors. If our assumptions prove to be incorrect, our allowance for loan losses may not be sufficient to cover losses inherent in our loan portfolio, resulting in additions to the allowance. Material additions to the allowance would materially decrease our net income.

Our emphasis on the origination of commercial real estate and business loans is one of the more significant factors in evaluating our allowance for loan losses. As we continue to increase the amount of these loans, additional or increased provisions for credit losses may be necessary and as a result would decrease our earnings.

We strive to maintain an appropriate allowance for loan and lease losses to provide for probable losses inherent in the loan portfolio. We periodically determine the amount of the allowance based on consideration of several factors such as default frequency, internal risk ratings, expected future cash collections, loss recovery rates and general economic factors, among others. Our methodology for measuring the adequacy of the allowance relies on several key elements, which include a specific allowance for identified problem loans and a general systematic allowance.

We believe our allowance for loan and lease losses is currently sufficient given the constant monitoring of the risk inherent in the loan portfolio. However, there is no precise method of predicting loan losses and therefore we always face the risk that charge-offs in future periods will exceed the allowance for loan and lease losses and that additional increases in the allowance for loan and lease losses will be required. In addition, the FDIC as well as the OCFI may require us to establish additional reserves. Additions to the allowance for loan and lease losses would result in a decrease of net earnings and capital, and could hinder our ability to pay dividends.

Given the severe economic conditions in Puerto Rico, we may continue to experience increased credit costs or need to take greater than anticipated markdowns and make greater than anticipated provisions to increase the allowances for loan losses on the loans acquired that could adversely affect our financial condition and results of operations in the future.

Bank regulators periodically review our allowance for loan losses and may require us to increase our provision for credit losses or loan charge-offs. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory authorities could have a materially adverse effect on our results of operations and/or financial condition.

Non-Compliance with USA Patriot Act, Bank Secrecy Act, or other laws and regulations could result in fines or sanctions.

Financial Institutions are required under the USA Patriot Act and Bank Secrecy Acts to develop programs to prevent financial institutions from being used for money-laundering and terrorist activities. Financial institutions are obligated to file suspicious activity reports with the U.S. Treasury Department's Office of Financial Crimes Enforcement Network if such activities are detected. These rules also require financial institutions to establish procedures for identifying and verifying the identity of customers seeking to open new financial accounts. Failure or the inability to comply with these regulations could result in enforcement actions, fines or

penalties, curtailment of expansion opportunities, intervention or sanctions by regulators or costly litigation or expensive additional controls and systems. We have developed policies and continue to augment procedures, staff and systems designed to assist in compliance with such laws and regulations.

We are subject to default and other risks in connection with mortgage loan originations.

From the time that we fund the mortgage loans originated to the time that they are sold, we are generally at risk for any mortgage loan defaults. Once we sell the mortgage loans, the risk of loss from mortgage loan defaults and foreclosures passes to the purchaser or insurer of the mortgage loans. However, in the ordinary course of business, we make representations and warranties to the purchasers and insurers of mortgage loans relating to the validity of such loans. If there is a breach of any of these representations or warranties, we may be required to repurchase the mortgage loan and bear any subsequent loss on the mortgage loan. We also may be required to repurchase mortgage loans in the event that there was improper underwriting or fraud or in the event that the loans become delinquent shortly after they are originated. For the year ended December 31, 2015, we repurchased \$26.6 million of loans from GNMA and FNMA. Any such repurchases in the future may negatively impact our liquidity and operating results. Termination of our ability to sell mortgage products to the U.S government-sponsored entities would have a material adverse effect on our results of operations and financial condition. In addition, we may be required to indemnify certain purchasers and others against losses they incur in the event of breaches of representations and warranties and in various other circumstances, including securities fraud claims, and the amount of such losses could exceed the purchase amount of the related loans. Consequently, we may be exposed to credit risk associated with sold loans. In addition, we incur higher liquidity risk with respect to mortgage loans not eligible to be purchased or insured by FNMA, GNMA or FHLMC, due to a lack of secondary market in which to sell these loans.

We have established reserves in our consolidated financial statements for potential losses that are considered to be both probable and reasonably estimable related to the mortgage loans sold by us. The adequacy of the reserve and the ultimate amount of losses incurred will depend on, among other things, the actual future mortgage loan performance, the actual level of future repurchase and indemnification requests, the actual success rate of claimants, developments in litigation related to us and the industry, actual recoveries on the collateral and macroeconomic conditions (including unemployment levels and housing prices). Due to uncertainties relating to these factors, there can be no assurance that our reserves will be adequate or that the total amount of losses incurred will not have a material adverse effect upon our financial condition or results of operations. For additional information related to our allowance for loan and lease losses, see “Note 6—Allowance for Loan and Lease Losses” to our audited consolidated financial statements included in this annual report on Form 10-K.

A prolonged economic downturn or recession or a continuing decline in the real estate market would likely result in an increase in delinquencies, defaults and foreclosures and in a reduction in loan origination activity, which would adversely affect our financial results.

The residential mortgage loan origination business has historically been cyclical, enjoying periods of strong growth and profitability followed by periods of lower volumes and industry-wide losses. The market for residential mortgage loan originations in Puerto Rico is currently in decline, and this trend could also reduce the level of mortgage loans that we may originate in the future and may adversely impact our business. During periods of rising interest rates, refinancing originations for many mortgage products tend to decrease as the economic incentives for borrowers to refinance their existing mortgage loans are reduced. In addition, the residential mortgage loan origination business is impacted by home values. A significant trend of decreasing values in several housing segments in Puerto Rico has also been noted. There is a risk that a reduction in housing values could negatively impact our loss levels on the mortgage loan portfolio because the value of the homes underlying the loans is a primary source of repayment in the event of foreclosure.

The decline in Puerto Rico's economy has had an adverse effect in the credit quality of our loan portfolios. Among other things, during the ongoing recession, we have experienced an increase in the level of non-performing assets and loan loss provision, which adversely affected our profitability. Although the delinquency rates have decreased recently, they may increase if the recession continues or worsens. If there is another decline in economic activity, additional increases in the allowance for loan and lease losses could be necessary with further adverse effects on our profitability.

Any sustained period of increased delinquencies, foreclosures or losses could harm our ability to sell loans, the price received on the sale of such loans, and the value of the mortgage loan portfolio, all of which could have a negative impact on our results of operations

and financial condition. In addition, any material decline in real estate values would weaken our collateral loan-to-value ratios and increase the possibility of loss if a borrower defaults. For a discussion of the impact of the Puerto Rico economy on our business operations, see “Most of our business is conducted in Puerto Rico, which is experiencing a deep economic recession, downturn in the real estate market, and a government fiscal and liquidity crisis.”

We are subject to security and operational risk related to our use of technology, including the risk of cyber-attack or cyber theft

Our operations rely on the secure processing, transmission and storage of confidential information in our computer systems and networks regarding our customers and their accounts. To provide these products and services, we use information systems and infrastructure that we and third party service providers operate. As a financial institution, we also are subject to and examined for compliance with an array of data protection laws, regulations and guidance, as well as to our own internal privacy and information security policies and programs.

Such incidents may include unauthorized access to our digital systems for purposes of misappropriation of assets, gaining access to sensitive information, corrupting data, or causing operational disruption. Although our information technology structure continue to be subject to cyber attacks, we have not experience a breach of cyber-security. Such an event could compromise our confidential information as well as that of our customers and third parties with whom we interact with and may result in negative consequences, including remediation costs, loss of revenues, additional regulatory scrutiny, litigation and reputational damage. Though we have insurance against some cyber-risks and attacks, it may not be sufficient to offset the impact of a material loss event.

While we have policies and procedures designated to prevent or limit the effect of the possible security breach of our information systems, if unauthorized persons were somehow to get access to confidential or proprietary information in our possession or to our proprietary information, it could result in significant legal and financial exposure, damage to our reputation or a loss of confidence in the security of our systems that could adversely affect our business. Though we have insurance against some cyber-risks and attacks, it may not be sufficient to offset the impact of a material loss event.

We rely on the services of third parties for our banking, information technology, telecommunications, and mortgage loan servicing infrastructure, and any failure, interruption or termination of such services or systems could have a material adverse affect on our financial condition and results of operations.

Our business relies on the secure, successful and uninterrupted functioning of our banking, information technology, telecommunications, and mortgage loan servicing infrastructure. We outsource some of our major systems, such as customer data and deposit processing, mortgage loan servicing, Internet and mobile banking, and electronic fund

transfer systems. The failure or interruption of such systems, or the termination of a third-party software license or mortgage servicing, or any service agreement on which any of these systems or services is based, could interrupt our operations. Because our information technology and telecommunications systems interface with and depend on third-party systems, we could experience service denials if demand for such services exceeds capacity or such systems fail or experience interruptions.

We periodically sell or securitize our mortgage loans while retaining the obligation to perform the servicing of such loans. Although we are the master servicer of our mortgage loan portfolios, we outsource our servicing functions pursuant to a subservicing arrangement with a third party in Puerto Rico. The termination or interruption of such subservicing arrangement, without a feasible substitute or successor, could adversely affect our financial condition and results of operations. In addition, because the FDIC has the right to refuse or delay payment for loan and lease losses if the shared-loss agreements are not performed by us in accordance with their terms, any such termination or interruption of the subservicing of the covered loans that we acquired in the FDIC-assisted acquisition could adversely affect our ability to comply with such terms.

If sustained or repeated, a failure, denial or termination of such systems or services could result in a deterioration of our ability to process new loans, service existing loans, gather deposits and/or provide customer service. It could also compromise our ability to operate effectively, damage our reputation, result in a loss of customer business and/or subject us to additional regulatory scrutiny and possible financial liability. Any of the foregoing could have a material adverse effect on our financial condition and results of operations.

Our financial results are constantly exposed to market risk, in particular to changes in interest rates.

Market risk refers to the probability of variations in the net interest income or the fair value of assets and liabilities due to changes in interest rates, currency exchange rates or equity prices.

Changes in interest rates are one of the principal market risks affecting us. Our income and cash flows depend to a great extent on the difference between the interest rates earned on interest-earning assets, such as loans and investment securities, and the interest rates paid on interest-bearing liabilities, such as deposits and borrowings. Net interest income is the difference between the revenue generated on interest-earning assets and the interest cost of funding those assets. Depending on the duration and repricing characteristics of the assets, liabilities and off-balance sheet items, changes in interest rates could either increase or decrease the level of net interest income. For any given period, the pricing structure of the assets and liabilities is matched when an equal amount of such assets and liabilities mature or reprice in that period.

We use an asset-liability management software program to project future movements in the balance sheet and income statement. The starting point of the projections generally corresponds to the actual values of the balance sheet on the date of the simulations. These simulations are highly complex and use many simplifying assumptions. In addition, the interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions and the policies of various governmental and regulatory agencies, in particular, the Federal Reserve Board. Changes in monetary policy, including changes in interest rates, will influence the origination of loans, the prepayment speed of loans, the value of loans and investment securities, the purchase of investments, the generation of deposits and the rates received on loans and investment securities and paid on deposits or other sources of funding.

We are subject to interest rate risk because of the following factors:

- Assets and liabilities may mature or reprice at different times. For example, if assets reprice slower than liabilities and interest rates are generally rising, earnings may initially decline.
- Assets and liabilities may reprice at the same time but by different amounts. For example, when the general level of interest rates is rising, we may increase rates charged on loans by an amount that is less than the general increase in market interest rates because of intense pricing competition. Also, basis risk occurs when assets and liabilities have similar repricing frequencies but are tied to different market interest rate indices that may not move in tandem.
- Short-term and long-term market interest rates may change by different amounts, *i.e.*, the shape of the yield curve may affect new loan yields and funding costs differently.
- The remaining maturity of various assets and liabilities may shorten or lengthen as interest rates change. For example, if long-term mortgage interest rates decline sharply, our mortgage-backed securities portfolios may prepay significantly earlier than anticipated, which could reduce portfolio income. If prepayment rates increase, we would be required to amortize net premiums into income over a shorter period of time, thereby reducing the corresponding asset yield and net interest income. Prepayment risk also has a significant impact on mortgage-backed securities and collateralized mortgage obligations since prepayments could shorten the weighted average life of these portfolios.
- Interest rates may have an indirect impact on loan demand, credit losses, loan origination volume, the value of financial assets and financial liabilities, gains and losses on sales of securities and loans, the value of mortgage

servicing rights and other sources of earnings.

In limiting interest rate risk to an acceptable level, management may alter the mix of floating and fixed rate assets and liabilities, change pricing schedules, adjust maturities through sales and purchases of investment securities, and enter into derivative contracts, among other alternatives. We may suffer losses or experience lower spreads than anticipated in initial projections as management implements strategies to reduce future interest rate exposure.

The hedging transactions that we enter into may not be effective in managing our exposure to market risk, including interest rate risk.

We use over-the-counter (“OTC”) derivatives, such as interest rate swaps and options on interest rate swaps, to manage part of our exposure to market risk caused by changes in interest rates. We have offered certificates of deposit with an option tied to the performance of the Standard & Poor 500 stock market index and use derivatives, such as option agreements with major broker-dealer companies, to manage our exposure to changes in the value of the index. The OTC derivative instruments that we may utilize also have their own risks, which include: (i) basis risk, which is the risk of loss associated with variations in the spread between the asset yield and the funding and/or hedge cost; (ii) credit or default risk, which is the risk of insolvency or other inability of the counterparty to a particular transaction to perform its obligations thereunder; and (iii) legal risk, which is the risk that we are unable to enforce certain terms of such instruments. All or any of such risks could expose us to losses. Further, as a result of the new regulatory regime

for OTC derivatives enacted under the Dodd-Frank Act, and the regulations issued thereunder by the SEC and the Commodity Futures Trading Commission, we are subject to additional reporting, recordkeeping and other requirements in connection with our use of OTC derivatives.

If the counterparty to an OTC derivative contract fails to perform, our credit risk is equal to the net fair value of the contract. We deal with counterparties that have high quality credit ratings at the time we enter into the counterparty relationships. However, there can be no assurances that the counterparties will have the ability to perform under their contracts. If the counterparty fails to perform, including as a result of the bankruptcy or insolvency of such counterparty, we would incur losses as a result.

Our business could be adversely affected if we cannot maintain access to stable funding sources.

Our business requires continuous access to various funding sources. We are able to fund our operations through deposits as well as through advances from the FHLB-NY and FRB-NY; however, our business is significantly dependent upon other wholesale funding sources, such as repurchase agreements and brokered deposits, which consisted of approximately 23% of our total interest-bearing liabilities as of December 31, 2015.

Brokered deposits are typically sold through an intermediary to small retail investors. Our ability to continue to attract brokered deposits is subject to variability based upon a number of factors, including volume and volatility in the global securities markets, our credit rating and the relative interest rates that we are prepared to pay for these liabilities. Brokered deposits are generally considered a less stable source of funding than core deposits obtained through retail bank branches. Investors in brokered deposits are generally more sensitive to interest rates and will generally move funds from one depository institution to another based on small differences in interest rates offered on deposits.

We expect to have continued access to credit from the foregoing sources of funds. However, there can be no assurance that such financing sources will continue to be available or will be available on favorable terms. In a period of financial disruption, or if negative developments occur with respect to us, the availability and cost of funding sources could be adversely affected. In that event, our cost of funds may increase, thereby reducing the net interest income, or we may need to dispose of a portion of the investment portfolio, which, depending upon market conditions, could result in realizing a loss or experiencing other adverse accounting consequences upon the dispositions. The interest rates that we pay on our securities are also influenced by, among other things, applicable credit ratings from recognized rating agencies. A downgrade to any of these credit ratings could affect our ability to access the capital markets, increase our borrowing costs and have a negative impact on our results of operations. Our efforts to monitor and manage liquidity risk may not be successful to deal with dramatic or unanticipated changes in the global securities markets or other reductions in liquidity driven by us or market related events. In the event that such sources of funds are reduced or eliminated and we are not able to replace them on a cost-effective basis, we may be forced to curtail or cease our loan origination business and treasury activities, which would have a material adverse effect on our operations and financial condition.

Our risk management policies, procedures and systems may be inadequate to mitigate all risks inherent in our various businesses.

A comprehensive risk management function is essential to the financial and operational success of our business. The types of risk we monitor and seek to manage include, but are not limited to, operational risk, technological and organizational risk, market risk, fiduciary risk, legal and compliance risk, liquidity risk and credit risk. We have adopted various policies, procedures and systems to monitor and manage these risks. There can be no assurance that those policies, procedures and systems are adequate to identify and mitigate all risks inherent in our various businesses. Our businesses and the markets in which we operate are also continuously evolving. If we fail to fully understand the implications of changes in our business or the financial markets and to adequately or timely enhance the risk framework to address those changes, we could incur losses. In addition, in a difficult or less liquid market environment, our risk management strategies may not be effective because other market participants may be attempting to use the same or similar strategies to deal with the challenging market conditions. In such circumstances, it may be difficult for us to reduce our risk positions due to the activity of such other market participants.

Competition with other financial institutions could adversely affect our profitability.

We face substantial competition in originating loans and in attracting deposits and assets to manage. The competition in originating loans and attracting assets comes principally from other U.S., Puerto Rico and foreign banks, investment advisors, securities broker-dealers, mortgage banking companies, consumer finance companies, credit unions, insurance companies, and other institutional lenders and purchasers of loans. We will encounter greater competition as we expand our operations. Increased competition may require us to increase the rates paid on deposits or lower the rates charged on loans which could adversely affect our profitability.

We operate in a highly regulated environment and may be adversely affected by changes in federal and local laws and regulations.

Our operations are subject to extensive regulation by federal and local governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of our operations. Because our business is highly regulated, the laws, rules and regulations applicable to us are subject to regular modification and change. For example, the Dodd-Frank Act has a broad impact on the financial services industry, including significant regulatory and compliance changes, as discussed under the subheading “Dodd-Frank Wall Street Reform and Consumer Protection Act” in Item 1 of this annual report.

The changes resulting from the Dodd-Frank Act may impact the profitability of our business activities, require changes to certain of our business practices, impose upon us more stringent capital, liquidity and leverage ratio requirements or otherwise adversely affect our business. In particular, the potential impact of the Dodd-Frank Act on our operations and activities, both currently and prospectively, include, among others:

- a reduction in our ability to generate or originate revenue-producing assets as a result of compliance with heightened capital standards;
- increased cost of operations due to greater regulatory oversight, supervision and examination of banks and bank holding companies, and higher deposit insurance premiums;
- the limitation on our ability to raise capital through the use of trust preferred securities as these securities will no longer be included as tier 1 capital going forward; and
- the limitation on our ability to expand consumer product and service offerings due to stricter consumer protection laws and regulations.

Further, we may be required to invest significant management attention and resources to evaluate and make necessary changes in order to comply with new statutory and regulatory requirements. Failure to comply with the new requirements may negatively impact our results of operations and financial condition. While we cannot predict what effect any presently contemplated or future changes in the laws or regulations or their interpretations would have on us, these changes could be materially adverse to our investors.

Legislative and other measures that may be taken by Puerto Rico governmental authorities could materially increase our tax burden or otherwise adversely affect our financial condition, results of operations or cash flows.

In an effort to address the Commonwealth’s ongoing fiscal problems, the Government has enacted tax reform in the past and is expected to do so in the future. In 2014, the Government of Puerto Rico approved an amendment to the Internal Revenue Code, which, among other things, changed the income tax rate for capital gains from 15% to 20%. In addition, in May 2015, the Government approved an increase in the state sales and use tax rate, effective July 1, 2015, from 6% to 10.5% (the municipal sales and use tax remained at a 1% rate), expanded the sales and use tax to certain

business-to-business services that were previously exempt, and provided for a transition to a value-added tax was expected to become effective on April 1, 2016. Now, the value added tax is expected to become effective on June 1, 2016. Legislative changes, particularly changes in tax laws, could adversely impact our results of operations.

We operate the IBE Unit and IBE Subsidiary pursuant to the IBE Act that provide us with significant tax advantages. An IBE has the benefits of exemptions from Puerto Rico income taxes on interest earned on, or gain realized from the sale of, non-Puerto Rico assets, including U.S. government obligations and certain mortgage-backed securities. This exemption has allowed us to have effective tax rates significantly below the maximum statutory tax rates. In the past, the Legislature of Puerto Rico has considered proposals to curb the tax benefits afforded to IBEs. In 2012, a new Puerto Rico law was enacted in this area. Although it did not repeal the IBE Act, the new law does not allow new license applications under the IBE Act to organize and operate an IBE. Any newly organized entity (now called an “international financial entity”) must be licensed under the new law and such entity (as opposed to existing IBEs organized under the IBE Act, including the Bank’s IBE Unit and IBE Subsidiary, which are “grandfathered”) will generally be subject to a 4% Puerto Rico income tax rate. In the event other legislation is passed in Puerto Rico to eliminate or modify the tax exemption enjoyed by IBEs, the consequences could have a materially adverse impact on us, including increasing the tax burden or otherwise adversely affecting our financial condition, results of operations or cash flows.

Our goodwill and other intangible assets could be determined to be impaired in the future and could decrease the Company’s earnings.

We are required to test our goodwill, core deposit and customer relationship intangible assets for impairment on a periodic basis. The impairment testing process considers a variety of factors, including the current market price of our common shares, the estimated net present value of our assets and liabilities, and information concerning the terminal valuation of similarly situated insured depository institutions. If an impairment determination is made in a future reporting period, our earnings and the book value of these intangible assets will be reduced by the amount of the impairment. If an impairment loss is recorded, it will have little or no impact on the tangible book value of our common shares or our regulatory capital levels, but such an impairment loss could significantly restrict the Company's ability to make dividend payments without prior regulatory approval.

Based on our annual goodwill impairment test, we determined that no impairment charges were necessary. As of December 31, 2015, we had on our consolidated balance sheet \$86.1 million of goodwill in connection with the BBVAPR Acquisition and the FDIC-assisted Eurobank acquisition, \$5.3 million of core deposit intangible in connection with the FDIC-assisted Eurobank acquisition and the BBVAPR Acquisition, and \$2.5 million of customer relationship intangible in connection with the BBVAPR Acquisition. There can be no assurance that future evaluations of such goodwill or intangibles will not result in any impairment charges. Among other factors, further declines in our common stock as a result of macroeconomic conditions and the general weakness of the Puerto Rico economy, could lead to an impairment of such assets. If such assets become impaired, it could have a negative impact on our results of operations.

Our ability to receive dividends from our subsidiaries could affect our liquidity and ability to pay dividends.

We are a separate and distinct legal entity from our subsidiaries. Dividends to us from our subsidiaries have represented a major source of funds for us to pay dividends on our common and preferred stock, make payments on corporate debt securities and meet other obligations. There are various U.S. federal and Puerto Rico law limitations on the extent to which Oriental Bank, our main subsidiary, can finance or otherwise supply funds to us through dividends and loans. These limitations include minimum regulatory capital requirements, U.S. federal and Puerto Rico banking law requirements concerning the payment of dividends out of net profits or surplus, Sections 23A and 23B of the Federal Reserve Act of 1913 and Regulation W of the Federal Reserve Board governing transactions between an insured depository institution and its affiliates, as well as general federal regulatory oversight to prevent unsafe or unsound practices. Further, under the new capital rules adopted by the federal banking regulatory agencies, a banking organization will need to hold a capital conservation buffer (composed of common equity tier 1 capital) greater than 2.5% of total risk-weighted assets to avoid limitations on capital distributions and discretionary bonus payments. Compliance with the capital conservation buffer is determined as of the end of the calendar quarter prior to any such capital distribution or discretionary bonus payment, and is subject to a three-year transition period beginning in 2016.

If our subsidiaries' earnings are not sufficient to make dividend payments while maintaining adequate capital levels, our liquidity may be affected, and we may not be able to make dividend payments to our holders of common and preferred stock or payments on outstanding corporate debt securities or meet other obligations, each of which could have a material adverse impact on our results of operations, financial position or perception of financial health.

In addition, our right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors.

Changes in accounting standards issued by the Financial Accounting Standards Board ("FASB") or other standard-setting bodies may adversely affect our financial statements.

Our financial statements are subject to the application of GAAP, which are periodically revised and/or expanded. Accordingly, from time to time we are required to adopt new or revised accounting standards issued by FASB. Market conditions have prompted accounting standard setters to promulgate new guidance which further interprets or seeks to revise accounting pronouncements related to financial instruments, structures or transactions as well as to issue new standards expanding disclosures. See "Note 1—Summary of Significant Accounting Policies" to our consolidated financial statements included herein for a discussion of any accounting developments that have been issued but not yet implemented. An assessment of proposed standards is not provided as such proposals are subject to change through the exposure process and, therefore, the effects on our consolidated financial statements cannot be meaningfully assessed. It is possible that future accounting standards that we are required to adopt could change the current accounting treatment that applies to the consolidated financial statements and that such changes could have a material effect on our financial condition and results of operations.

Competition in attracting talented people could adversely affect our operations.

We depend on our ability to attract and retain key personnel and we rely heavily on our management team. The inability to recruit and retain key personnel or the unexpected loss of key managers may adversely affect our operations. Our success to date has been influenced strongly by the ability to attract and retain senior management experienced in banking and financial services. Retention of senior managers and appropriate succession planning will continue to be critical to the successful implementation of our strategies.

Reputational risk and social factors may impact our results.

Our ability to originate loans and to attract deposits and assets is highly dependent upon the perceptions of consumer, commercial and funding markets of our business practices and our financial health. Negative public opinion could result from actual or alleged conduct in any number of activities or circumstances, including lending practices, regulatory compliance, inadequate protection of customer information, or sales and marketing, and from actions taken by regulators in response to such conduct. Adverse perceptions regarding us could lead to difficulties in originating loans and generating and maintaining accounts as well as in financing them.

In addition, a variety of social factors may cause changes in borrowing activity, including credit card use, payment patterns and the rate of defaults by account holders and borrowers. If consumers develop or maintain negative attitudes about incurring debt, or if consumption trends decline, our business and financial results will be negatively affected.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company owns a fifteen-story office building located at 254 Muñoz Rivera Avenue, San Juan Puerto Rico, known as Oriental Center. The Company operates a full service branch at the plaza level and our centralized units and subsidiaries occupy approximately 66% of the office floor space. Approximately 34% of the office space is leased to outside tenants. The Company also leases offices at 997 San Roberto Street, Professional Offices Park, San Juan, Puerto Rico, known as Oriental Tower. In addition, the Company also leases an office space in Boca Raton, Florida for the operations of OPC, its retirement plan administrator.

The Bank owns ten branch premises and leases thirty eight branch commercial offices throughout Puerto Rico. The Bank's management believes that each of its facilities is well maintained and suitable for its purpose and can readily obtain appropriate additional space as may be required at competitive rates by extending expiring leases or finding alternative space.

At December 31, 2015, the aggregate future rental commitments under the terms of the leases, exclusive of taxes, insurance and maintenance expenses payable by the Company, was \$45.3 million.

The Company's investment in premises and equipment, exclusive of leasehold improvements at December 31, 2015, was \$106.9 million, gross of accumulated depreciation.

ITEM 3. LEGAL PROCEEDINGS

The Company and its subsidiaries are defendants in a number of legal proceedings incidental to their business. The Company is vigorously contesting such claims. Based upon a review by legal counsel and the development of these matters to date, management is of the opinion that the ultimate aggregate liability, if any, resulting from these claims will not have a material adverse effect on the Company's financial condition or results of operations.

ITEM 4. MINE SAFETY DISCLOSURE

Not applicable.

PART II

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

The Company's common stock is traded on the New York Stock Exchange ("NYSE") under the symbol "OFG". Information concerning the range of high and low sales prices for the Company's common stock for each quarter in the years ended December 31, 2015 and 2014, as well as cash dividends declared for such periods is set forth under the sub-heading "Stockholders' Equity" in the "Analysis of Financial Condition" caption in the Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A").

Information concerning legal or regulatory restrictions on the payment of dividends by the Company and the Bank is contained under the sub-heading "Dividend Restrictions" in Item 1 of this report.

As of December 31, 2015, the Company had approximately 2,999 holders of record of its common stock, including all directors and officers of the Company, and beneficial owners whose shares are held in "street" name by securities broker-dealers or other nominees.

Stock Performance Graph

The graph below compares the percentage change in the Company's cumulative total stockholder return during the measurement period with the cumulative total return, assuming reinvestment of dividends, of the Russell 2000 Index and the SNL Bank Index.

The cumulative total stockholder return was obtained by dividing the sum of (i) the cumulative amount of dividends per share, assuming dividend reinvestment, for the measurement period beginning December 31, 2010, and (ii) the difference between the share price at the beginning and the end of the measurement period, by the share price at the beginning of the measurement period.

*Comparison of 5 Year Cumulative Total Return**Assumes Initial Investment of \$100*

Index	12/31/2010	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015
OFG Bancorp	100.00	98.78	111.17	146.65	143.69	65.22
Russell 2000	100.00	95.82	111.49	154.78	162.35	155.18
SNL Bank	100.00	77.44	104.51	143.49	160.40	163.14

ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” under Item 7 and “Financial Statements and Supplementary Data” under Item 8 of this report.

OFG Bancorp
SELECTED FINANCIAL DATA
YEARS ENDED DECEMBER 31, 2015, 2014, 2013, 2012, AND 2011

	Year Ended December 31,				
	2015	2014	2013	2012	2011
EARNINGS DATA:	(In thousands, except per share data)				
Interest income	\$ 406,568	\$ 485,257	\$ 493,632	\$ 260,808	\$ 297,295
Interest expense	69,196	76,782	83,960	103,518	156,362
Net interest income	337,372	408,475	409,672	157,290	140,933
Provision for loan and lease losses	161,501	60,640	72,894	23,681	13,813
Net interest income after provision for loan and leases lossess	175,871	347,835	336,778	133,609	127,120
Non-interest income	52,472	17,323	17,095	26,057	32,241
Non-interest expenses	248,401	242,725	264,136	131,810	124,045
(Loss) income before taxes	(20,058)	122,433	89,737	27,856	35,316
Income tax (benefit) expense	(17,554)	37,252	(8,709)	3,301	866
Net (loss) income	(2,504)	85,181	98,446	24,555	34,450
Less: dividends on preferred stock	(13,862)	(13,862)	(13,862)	(9,939)	(4,802)
(Loss) income available to common shareholders	\$ (16,366)	\$ 71,319	\$ 84,584	\$ 14,616	\$ 29,648
PER SHARE DATA:					
Basic	\$ (0.37)	\$ 1.58	\$ 1.85	\$ 0.35	\$ 0.67
Diluted	\$ (0.37)	\$ 1.50	\$ 1.73	\$ 0.35	\$ 0.67
Average common shares outstanding	51,455	45,024	45,706	41,626	44,433
Average common shares outstanding and equivalents	44,231	52,326	53,033	45,304	44,524
Book value per common share	\$ 16.67	\$ 17.40	\$ 15.74	\$ 15.31	\$ 15.28
Tangible book value per common share	\$ 14.53	15.25	13.60	13.10	\$ 15.19
Market price at end of period	\$ 7.32	16.65	17.34	13.35	\$ 12.11
Cash dividends declared per common share	\$ 0.36	0.34	0.26	0.24	\$ 0.21
Cash dividends declared on common shares	\$ 15,932	15,286	11,875	10,067	\$ 9,153
PERFORMANCE RATIOS:					
Return on average assets (ROA)	-0.03%	1.10%	1.15%	0.37%	0.48%
Return on average tangible common stockholders' equity	-2.47%	10.91%	14.01%	2.32%	4.54%
Return on average common equity (ROE)	-2.16%	9.50%	12.03%	2.29%	4.50%
Equity-to-assets ratio	12.64%	12.65%	10.85%	9.38%	10.38%
Efficiency ratio	60.00%	49.90%	53.45%	64.05%	66.26%
Interest rate spread	4.95%	5.79%	5.46%	2.59%	2.15%

Interest rate margin	5.03%	5.84%	5.46%	2.67%	2.19%
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PERIOD END BALANCES AND CAPITAL RATIOS:	December 31,				
	2015	2014	2013	2012	2011
	(In thousands, except per share data)				
Investments and loans					
Investment securities	\$ 1,615,872	\$ 1,402,056	\$ 1,614,809	\$ 2,233,265	\$ 3,867,970
Originated loans, net	3,016,781	2,811,207	2,400,023	1,278,750	1,169,916
Acquired loans, net	1,417,432	2,015,439	2,619,396	3,878,887	496,276
Total investments and loans	\$ 6,050,085	\$ 6,228,702	\$ 6,634,228	\$ 7,390,902	\$ 5,534,162
Deposits and borrowings					
Deposits	\$ 4,716,859	\$ 4,924,406	\$ 5,383,265	\$ 5,690,579	\$ 2,437,796
Securities sold under agreements to repurchase	934,691	980,087	1,267,618	1,695,247	3,056,238
Other borrowings	436,843	439,919	439,816	791,417	427,063
Total deposits and borrowings	\$ 6,088,393	\$ 6,344,412	\$ 7,090,699	\$ 8,177,243	\$ 5,921,097
Stockholders' equity					
Preferred stock	\$ 176,000	\$ 176,000	\$ 176,000	\$ 176,000	\$ 68,000
Common stock	52,626	52,626	52,707	52,671	47,809
Additional paid-in capital	540,512	539,311	538,071	537,453	499,096
Legal surplus	70,435	70,435	61,957	52,143	50,178
Retained earnings	148,886	181,184	133,629	70,734	68,149
Treasury stock, at cost	(105,379)	(97,070)	(80,642)	(81,275)	(74,808)
Accumulated other comprehensive income	13,997	19,711	3,191	55,880	37,131
Total stockholders' equity	\$ 897,077	\$ 942,197	\$ 884,913	\$ 863,606	\$ 695,555
Capital ratios					
Leverage capital	11.18%	10.61%	9.06%	6.55%	9.65%
Tier 1 common equity to risk-weighted assets	N/A	11.88%	10.46%	8.76%	27.01%
Common equity Tier 1 capital ratio	12.14%	N/A	N/A	N/A	N/A
Tier 1 risk-based capital	15.99%	16.02%	14.38%	13.18%	31.84%
Total risk-based capital	17.29%	17.57%	16.16%	15.40%	33.12%
Financial assets managed					
Trust assets managed	\$ 2,691,423	\$ 2,841,111	\$ 2,796,923	\$ 2,514,401	\$ 2,216,088
Broker-dealer assets gathered	2,374,709	2,622,001	2,493,324	2,722,197	1,926,148
Total assets managed	\$ 5,066,132	\$ 5,463,112	\$ 5,290,247	\$ 5,236,598	\$ 4,142,236

The ratios shown below demonstrate the Company's ability to generate sufficient earnings to pay the fixed charges or expenses of its debt and preferred stock dividends. The Company's consolidated ratios of earnings to combined fixed charges and preferred stock dividends were computed by dividing earnings by combined fixed charges and preferred stock dividends, as specified below, using two different assumptions, one excluding interest on deposits and the second including interest on deposits:

	Year Ended December			
	2015	2014	2013	2012
Consolidated Ratios of Earnings to Combined Fixed Charges and Preferred Stock Dividends				
Excluding Interests on Deposits	(A) 2.81x	2.26x	1.2	
Including Interests on Deposits	(A) 2.16x	1.75x	1.15	

(A) In 2015, earnings were not sufficient to cover preferred stock dividends, and the ratio was less than 1:1. The Company would have had to generate additional earnings of \$34 million to achieve a ratio of 1:1 in 2015.

For purposes of computing these consolidated ratios, earnings represent income before income taxes plus fixed charges and amortization of capitalized interest, less interest capitalized. Fixed charges consist of interest expensed and capitalized, amortization of debt issuance costs, and the Company's estimate of the interest component of rental expense. The term "preferred stock dividends" is the amount of pre-tax earnings that is required to pay dividends on the Company's outstanding preferred stock. As of the dates presented above, except for 2011, the Company had noncumulative perpetual preferred stock issued and outstanding amounting to \$176.0 million, as follows: (i) Series A amounting to \$33.5 million or 1,340,000 shares at a \$25 liquidation value; (ii) Series B amounting to \$34.5 million or 1,380,000 shares at a \$25 liquidation value; (iii) Series C amounting to \$84.0 million or 84,000 shares at a \$1,000 liquidation value; and (iv) Series D amounting to \$24.0 million or 960,000 shares at a \$25 liquidation value. At December 31, 2011, the Company had noncumulative perpetual preferred stock issued and outstanding amounting to \$68.0 million, as follows: (i) Series A amounting to \$33.5 million or 1,340,000 shares at a \$25 liquidation value; (ii) Series B amounting to \$34.5 million or 1,380,000 shares at a \$25 liquidation value.

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
FOR THE YEAR ENDED DECEMBER 31, 2015**

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The accounting and reporting policies followed by the Company conform with GAAP and general practices within the financial services industry. The Company's significant accounting policies are described in detail in Note 1 to the consolidated financial statements and should be read in conjunction with this section.

Critical accounting policies require management to make estimates and assumptions, which involve significant judgment about the effect of matters that are inherently uncertain and that involve a high degree of subjectivity. These estimates are made under facts and circumstances at a point in time and changes in those facts and circumstances could produce actual results that differ from those estimates. The following MD&A section is a summary of what management considers the Company's critical accounting policies.

Loans and Leases

Originated and Other Loans and Leases Held in Portfolio

Loans the Company originates and intends to hold in portfolio are stated at the principal amount outstanding, adjusted for unamortized deferred fees and costs which are amortized to interest income over the expected life of the loan using the interest method. The Company discontinues accrual of interest on originated loans after payments become more than 90 days past due or earlier if the Company does not expect the full collection of principal or interest. The delinquency status is based upon the contractual terms of the loans.

Loans for which the recognition of interest income has been discontinued are designated as non-accruing. Collections are accounted for on the cash method thereafter, until qualifying to return to accrual status. Such loans are not reinstated to accrual status until interest is received on a current basis and other factors indicative of doubtful collection cease to exist generally for a period of six-months. The determination as to the ultimate collectability of the loan's balance may involve management's judgment in the evaluation of the borrower's financial condition and prospects for repayment.

The Company follows a systematic methodology to establish and evaluate the adequacy of the allowance for loan and lease losses to provide for inherent losses in the loan portfolio. This methodology includes the consideration of factors such as economic conditions, portfolio risk characteristics, prior loss experience, and results of periodic credit reviews of individual loans. The provision for loan and lease losses charged to current operations is based on such methodology. Loan and lease losses are charged and recoveries are credited to the allowance for loan and lease losses on originated and other loans.

Larger commercial loans that exhibit potential or observed credit weaknesses are subject to individual review and grading. Where appropriate, allowances are allocated to individual loans based on management's estimate of the borrower's ability to repay the loan given the availability of collateral, other sources of cash flow, and legal options available to the Company.

Included in the review of individual loans are those that are impaired. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or as a practical expedient, at the observable market price of the loan or the fair value of the collateral, if the loan is collateral dependent. Loans are individually evaluated for impairment, except large groups of small balance homogeneous loans that are collectively evaluated for impairment and loans that are recorded at fair value or at the lower of cost or fair value. The Company measures for impairment all commercial loans over \$250 thousand (i) that are either

over 90 days past due or adversely classified, or (ii) when deemed necessary by management and TDR's. The portfolios of mortgage loans, auto and leasing, and consumer loans are considered homogeneous and are evaluated collectively for impairment.

The Company uses a rating system to apply an overall allowance percentage to each originated and other loan portfolio segment based on historical credit losses adjusted for current conditions and trends. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over a determined look back period for each segment. The actual loss factor is adjusted by the appropriate loss emergence period as calculated for each portfolio. Then, the adjusted loss experience is supplemented with other qualitative factors based on the risks present for each portfolio segment. These qualitative factors include consideration of the following: the credit grading assigned to commercial loans; levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff, including the bank's loan review system as graded by regulatory agencies in their last examination; local economic trends and conditions; industry conditions; effects of external factors such as competition and regulatory requirements on the level of estimated credit losses in the current portfolio; and effects of changes in credit concentrations and collateral value. Additional impact from the historical loss experience is applied based on levels of delinquency and loan classification, and for the auto loan portfolio by FICO score.

At origination, a determination is made whether a loan will be held in our portfolio or is intended for sale in the secondary market. Loans that will be held in the Company's portfolio are carried at amortized cost. Residential mortgage loans held for sale are recorded at the lower of the aggregate cost or market value ("LOCOM").

Acquired Loans and Leases

Loans that the Company acquire in acquisitions are recorded at fair value with no carryover of the related allowance for loan losses. Determining the fair value of the loans involves estimating the amount and timing of principal and interest cash flows expected to be collected on the loans and discounting those cash flows at a market rate of interest.

The Company has acquired loans in two separate acquisitions, the BBVAPR Acquisition in December 2012 and the FDIC-assisted Eurobank acquisition in April 2010. For each acquisition, the Company considered the following factors as indicators that an acquired loan had evidence of deterioration in credit quality and was therefore in the scope of ASC 310-30:

- Loans that were 90 days or more past due,
- Loans that had an internal risk rating of substandard or worse. Substandard is consistent with regulatory definitions and is defined as having a well-defined weakness that jeopardizes liquidation of the loan,

- Loans that were classified as nonaccrual by the acquired bank at the time of acquisition, and
- Loans that had been previously modified in a troubled debt restructuring.

Any acquired loans that were not individually in the scope of ASC 310-30 because they did not meet the criteria above were either (i) pooled into groups of similar loans based on the borrower type, loan purpose, and collateral type and accounted for under ASC 310-30 by analogy or (ii) accounted for under ASC 310-20 (Non-refundable fees and other costs).

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

Revolving credit facilities such as credit cards, retail and commercial lines of credit and floor plans which are specifically scoped out of ASC 310-30 are accounted for under the provisions of ASC 310-20. Also, performing auto loans with FICO scores over 660 acquired at a premium in the BBVAPR Acquisition are accounted for under this guidance. Auto loans with FICO scores below 660 were acquired at a discount and are accounted for under the provisions of ASC 310-30. The provisions of ASC 310-20 require that any differences between the contractually required loan payments in excess of the Company's initial investment in the loans be accreted into interest income on a level-yield basis over the life of the loan. Loans acquired in the BBVAPR Acquisition that were accounted for under the provisions of ASC 310-20 which had fully amortized their premium or discount, recorded at the date of acquisition, are removed from the acquired loan category. Loans accounted for under ASC 310-20 are placed on non-accrual status when past due in accordance with the Company's non-accruing policy and any accretion of discount is discontinued. These assets were recorded at estimated fair value on their acquisition date, incorporating an estimate of future expected cash flows. Such fair value includes a credit discount which accounts for expected loan losses over the estimated life of these loans. Management takes into consideration this credit discount when determining the necessary allowance for acquired loans that are accounted for under the provisions of ASC 310-20.

The allowance for loan and lease losses model for acquired loans accounted for under ASC 310-20 is the same as for the originated and other loan portfolio.

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

The Company performed a fair market valuation of each of the loan pools, and each pool was recorded at a discount. The Company determined that at least part of the discount on the acquired individual or pools of loans was attributable to credit quality by reference to the valuation model used to estimate the fair value of these pools of loans. The valuation model incorporated lifetime expected credit losses into the loans' fair valuation in consideration of factors such as evidence of credit deterioration since origination and the amounts of contractually required principal and interest that the Company did not expect to collect as of the acquisition date. Based on the guidance included in the December 18, 2009 letter from the AICPA Depository Institutions Panel to the Office of the Chief Accountant of the SEC, the Company has made an accounting policy election to apply ASC 310-30 by analogy to all of these acquired pools of loans as they all (i) were acquired in a business combination or asset purchase, (ii) resulted in recognition of a discount attributable, at least in part, to credit quality; and (iii) were not subsequently accounted for at fair value.

The excess of expected cash flows from acquired loans over the estimated fair value of acquired loans at acquisition is referred to as the accretable discount and is recognized into interest income over the remaining life of the acquired loans using the interest method. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the nonaccretable discount. The nonaccretable discount represents estimated future credit losses expected to be incurred over the life of the acquired loans. Subsequent decreases to the expected cash flows require the Company to evaluate the need for an addition to the allowance for loan losses. Subsequent improvements in expected cash flows result in the reversal of the associated allowance for loan losses, if any and the reversal of a corresponding amount of the nonaccretable discount which the Company then reclassifies as accretable discount that is recognized into interest income over the remaining life of the loan using the interest method. The Company's evaluation of the amount of future cash flows that it expects to collect takes into account actual credit performance of the acquired loans to date and the Company's best estimates for the expected lifetime credit performance of the loans using currently available information. Charge-offs of the principal amount on acquired loans would be first applied to the nonaccretable discount portion of the fair value adjustment. To the extent that the Company experiences deterioration in credit quality in its expected cash flows subsequent to the acquisition of the loans; an allowance for loan losses would be established based on the estimate of future credit losses over the remaining life of the loans.

In accordance with ASC 310-30, recognition of income is dependent on having a reasonable expectation about the timing and amount of cash flows expected to be collected. The Company performs such an evaluation on a quarterly basis on both its acquired loans individually accounted for under ASC 310-30 and those in pools accounted for under ASC 310-30 by analogy.

Cash flows for acquired loans individually accounted for under ASC 310-30 are estimated on a quarterly basis. Based on this evaluation, a determination is made as to whether or not the Company has a reasonable expectation about the timing and amount of cash flows. Such an expectation includes cash flows from normal customer repayment, collateral value, foreclosure or other collection efforts. Cash flows for acquired loans accounted for on a pooled basis under ASC 310-30 by analogy are also estimated on a quarterly basis. For residential real estate, home equity and other consumer loans, cash flow loss estimates are calculated based on a model that incorporates a projected probability of default and loss. For commercial loans, lifetime loss rates are assigned to each pool with consideration given for pool make-up, including risk rating profile. Lifetime loss rates are developed from internally generated historical loss data and are applied to each pool.

To the extent that the Company cannot reasonably estimate cash flows, interest income recognition is discontinued. The unit of account for loans in pools accounted for under ASC 310-30 by analogy is the pool of loans. Accordingly, as long as the Company can reasonably estimate cash flows for the pool as a whole, accretable yield on the pool is recognized and all individual loans within the pool - even those more than 90 days past due - would be considered to be accruing interest in the Company's financial statement disclosures, regardless of whether or not the Company expects any principal or interest cash flows on an individual loan 90 days or more past due.

Because of the loss protection provided by the FDIC, the risk of the loans acquired in the FDIC-assisted Eurobank acquisition that are covered under the FDIC shared-loss agreements are significantly different from loans not covered under the FDIC shared-loss agreement. These loans are referred to as "covered loans". The FDIC shared-loss agreement related to the commercial and other non-single family acquired Eurobank loans expired on June 30, 2015. The coverage for single-family residential loans will expire on June 30, 2020. Covered loans are no longer a material amount. Therefore, the Company changed its current and prior year loan disclosures.

Covered loans are accounted for under ASC 310-30. To the extent credit deterioration occurs after the date of acquisition, the Company will record an allowance for loan and lease losses and an increase in the FDIC shared-loss indemnification asset for the expected reimbursement from the FDIC under the shared-loss agreement.

Allowance for Loan and Lease Losses for Originated and Acquired BBVAPR Loans and Leases

The Company follows a systematic methodology to establish and evaluate the adequacy of the allowance for loan and lease losses to provide for inherent losses in its loan portfolio. This methodology includes the consideration of factors such as economic conditions, portfolio risk characteristics, prior loss experience, and results of periodic credit reviews of individual loans.

The loss factor used for the general reserve of these loans is established considering the Bank's historical loss experience adjusted for an estimated loss emergence period and the consideration of environmental factors. Environmental factors considered are: changes in non-performing loans; migration in classification; trends in charge offs; trends in volume of loans; changes in collateral values; changes in risk selections and underwriting standards, and other changes in lending policies, procedures and practices; experience, ability and depth of lending management and other relevant staff, including the Company's loan review system; national and local economic trends and industry conditions; and effect of external factors such as competition and regulatory requirements on the level of estimated credit losses. The sum of the adjusted loss experience factors and the environmental factors will be the general valuation reserve ("GVA") factor to be used for the determination of the allowance for loan and lease losses in each category.

As part of the Company's continuous enhancement to the allowance for loan and lease losses methodology, during the year 2015 the following assumptions were reviewed:

- An assessment of the look-back period and historical loss factor was performed for all portfolio segments. The analysis was based on the trends observed and their relation with the economic cycle as of the period of the analysis. As a result, for the commercial portfolio, the look-back period was changed to 36 months from the previously determined 12 months. For auto, leasing and consumer, a look-back period of 24 months was maintained. The residential mortgages portfolio was evaluated during the fourth quarter of 2015. For this portfolio, a 12-month look-back period was maintained as management concluded that, given the charge offs evolution, a shorter period of losses is more representative of the recent trends and more accurate in predicting future losses

- During the second quarter of 2015, an assessment of environmental factors was performed for commercial, auto, and consumer portfolios. As a result, the environmental factors continue to reflect our assessment of the impact to our portfolio, taking into consideration the current evolution of the portfolios and expected impact, due to recent economic developments, changes in values of collateral and delinquencies, among others.

- During the fourth quarter of 2015 the loss realization period was revised to 1.60 years for commercial real estate, other portfolios remained at one year.

These changes in the allowance for loan and lease losses' look-back period and loss emergence period for the commercial portfolios are considered a change in accounting estimate as per ASC 250-10 provisions, where adjustments are made prospectively.

Originated and Other Loans and Leases Held for Investment and Acquired Loans Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)

The Company determines the allowance for loan and lease losses by portfolio segments, which consist of mortgage loans, commercial loans, consumer loans, and auto and leasing, as follows:

Mortgage loans: These loans are divided into four classes: traditional mortgages, non-traditional mortgages, loans in loan modification programs and home equity secured personal loans. Traditional mortgage loans include loans secured by a dwelling, fixed coupons and regular amortization schedules. Non-traditional mortgages include loans with interest-first amortization schedules and loans with balloon considerations as part of their terms. Mortgages in loan modification programs are loans that are being serviced under such programs. Home equity loans are mainly equity lines of credit. The allowance factor on these loans is impacted by the adjusted historical loss factors on the sub-segments and the environmental risk factors described above and by delinquency buckets. The traditional mortgage loan portfolio is further segregated by vintages and then by delinquency buckets.

Commercial loans: The commercial portfolio is segmented by business line (corporate, institutional, middle market, corporate retail, floor plan, and real estate) and by collateral type (secured by real estate and other commercial and industrial assets). The loss factor used for the GVA of these loans is established considering the Bank's past thirty-six month historical loss experience of each segment adjusted for the loss realization period and the consideration of environmental factors. The sum of the adjusted loss experience and the environmental factors is the GVA factor used for the determination of the allowance for loan and lease losses on each category.

Consumer loans: The consumer portfolio consists of smaller retail loans such as retail credit cards, overdrafts, unsecured personal lines of credit, and personal unsecured loans. The allowance factor, consisting of the adjusted historical loss factor and the environmental risk factors, will be calculated for each sub-class of loans by delinquency bucket.

Auto and Leasing: The auto and leasing portfolio consists of financing for the purchase of new or used motor vehicles for private or public use. These loans are granted mainly through dealers authorized and approved by the auto department credit committee of the Bank. In addition, this segment includes personal loans guaranteed by vehicles in the form of lease financing. The allowance factor on the auto and leasing portfolio is impacted by the adjusted historical loss factor and the environmental risk factors. For the determination of the allowance factor, the portfolio is segmented by FICO score, which is updated on a quarterly basis and then by delinquency bucket.

The Company establishes its allowance for loan losses through a provision for credit losses based on our evaluation of the credit quality of the loan portfolio. This evaluation, which includes a review of loans on which full collectability may not be reasonably assured, considers, among other matters, the estimated fair value of the underlying collateral, economic conditions, historical net loan loss experience, and other factors that warrant recognition in determining our allowance for loan losses. The Company continues to monitor and modify the level of the allowance for loan losses to ensure it is adequate to cover losses inherent in our loan portfolio.

Our allowance for loan losses consists of the following elements: (i) specific valuation allowances based on probable losses on specifically identified impaired loans; and (ii) valuation allowances based on net historical loan loss experience for similar loans with similar inherent risk characteristics and performance trends, adjusted, as appropriate, for qualitative risk factors specific to respective loan types.

When current information and events indicate that it is probable that we will be unable to collect all amounts of principal and interest due under the original terms of a business or commercial real estate loan greater than \$250 thousand, such loan will be classified as impaired. Additionally, all loans modified in a troubled debt restructuring ("TDR") are considered impaired. The need for specific valuation allowances are determined for impaired loans and recorded as necessary. For impaired loans, we consider the fair value of the underlying collateral, less estimated costs to sell, if the loan is collateral dependent, or we use the present value of estimated future cash flows in determining the

estimates of impairment and any related allowance for loan losses for these loans. Confirmed losses are charged off immediately. Prior to a loan becoming impaired, we typically would obtain an appraisal through our internal loan grading process to use as the basis for the fair value of the underlying collateral.

Loan loss ratios and credit risk categories are updated at least quarterly and are applied in the context of GAAP as prescribed by ASC and the importance of depository institutions having prudent, conservative, but not excessive loan allowances that fall within an acceptable range of estimated losses. While management uses current available information in estimating possible loan and lease losses, factors beyond the Company's control, such as those affecting general economic conditions, may require future changes to the allowance.

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

For our acquired loans accounted for under ASC Subtopic 310-30, our allowance for loan losses is estimated based upon our expected cash flows for these loans. To the extent that we experience a deterioration in borrower credit quality resulting in a decrease in the net present value of our expected cash flows (which are used as a proxy to identify probable incurred losses) subsequent to the acquisition of the loans, an allowance for loan losses is established based on our estimate of future credit losses over the remaining life of the loans.

Acquired loans accounted for under ASC 310-30 are not considered non-performing and continue to have an accretable yield as long as there is a reasonable expectation about the timing and amount of cash flows expected to be collected. Also, loans charged-off against the non-accretable difference established in purchase accounting are not reported as charge-offs. Charge-offs on loans

accounted under ASC Subtopic 310-30 are recorded only to the extent that losses exceed the non-accretable difference established with purchase accounting.

Covered loans are accounted for under ASC 310-30 and our policy is consistent with our policy for non-covered acquired loans. For covered loans, the portion of the loss reimbursable from the FDIC is recorded as an offset to the provision for credit losses and increases the FDIC shared-loss indemnification asset.

Financial Instruments

Certain financial instruments, including derivatives, trading securities and investment securities available-for-sale, are recorded at fair value and unrealized gains and losses are recorded in other comprehensive income or as part of non-interest income, as appropriate. Fair values are based on listed market prices, if available. If listed market prices are not available, fair value is determined based on other relevant factors, including price quotations for similar instruments. The fair values of certain derivative contracts are derived from pricing models that consider current market and contractual prices for the underlying financial instruments as well as time value and yield curve or volatility factors underlying the positions.

The Company determines the fair value of its financial instruments based on the fair value measurement framework, which establishes a fair value hierarchy that prioritizes the inputs of valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 — Level 1 assets and liabilities include equity securities that are traded in an active exchange market, as well as certain U.S. Treasury and other U.S. government agency securities that are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 — Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include (i) mortgage-backed securities for which the fair value is estimated based on valuations obtained from third-party pricing services for identical or comparable assets, (ii) debt securities with quoted prices that are traded less frequently than exchange-traded instruments and (iii) derivative contracts and financial liabilities whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

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

2015 FINANCIAL HIGHLIGHTS

For 2015, the Company reported a loss to common shareholders of \$16.4 million, or (\$0.37) per share, compared to income of \$71.3 million, or \$1.50 per diluted share, in 2014.

These results reflect the significant de-risking steps taken by the Company, including the following:

- Reduction in interest income as the balance of our loans to the Puerto Rico central government and its public corporations fell 47.8% to \$211.9 million at December 31, 2015, from \$406.1 million a year ago. Our loans to Puerto Rico municipalities declined 4.4% to \$203.5 million, and the balance of our Puerto Rico government securities decreased by 15.0% to \$17.8 million.
- An increase in share-loss amortization of \$10.2 million in the second quarter of 2015 upon successful negotiation and termination of the FDIC commercial shared loss coverage. However, this also resulted in a reduction of approximately \$10 million a quarter going forward, starting in the third quarter, for a total reduction of \$22.2 million in the year 2015.
- A successful bulk sale of \$235.2 million in unpaid principal balances of acquired non-performing assets ("NPAs"). This resulted in a charge of \$20.2 million pre-tax in 2015.
- The de-risking of the loan portfolio resulted in normalization of net interest margin to 5.03% from 5.84%, primarily reflecting contraction from the steep reduction in tax exempt, high-yield, government-related loans.
- A \$53.3 million provision for loan and lease losses on the \$200 million participation in a syndicated fuel line of credit to the PREPA, reflecting continued hurdles in restructuring the credit. Currently in non-accrual status, interest payments are being credited to the payment of principal, which now stands at \$137.0 million, net of allowances, or 68.5% of the outstanding principal balance.

Growth of the Oriental retail franchise through new customers, products and services.

- Oriental Bank furthered its innovative edge in the third quarter of 2015 with the launch of MyStatus. The industry-first mobile app updates home buyers on every step of their mortgage application from origination through closing.
- MyStatus followed the introduction of FOTOdepósito, People Pay, and Cuenta Libre (Freedom Account). With Cuenta Libre, customers who access their accounts via mobile phone, tablet, web, debit/credit card, or ATMs, do not have to pay ATM fees.
- Such products and services, among others, helped the Bank add 15,400 net new retail customers, increasing its total customer base by 4.40%. New customers added approximately \$67 million in deposits, \$115 million in loans, and \$15 million in wealth management assets.

○ In total, new loan production of \$1.0 billion increased 10.3% year over year, with commercial loans up 38.9%, residential mortgage loans up 14.8%, and consumer loans up 17.3%, more than offsetting a decline in auto loans.

All components of our business continued strong, given Puerto Rico's deep economic recession and severe fiscal crisis.

Interest Income

Total interest income for 2015 decreased 16.2% to \$406.6 million when compared to \$485.3 million for 2014, reflecting the transition in our loan portfolio as originated loans with normal yields grow and higher-yielding acquired loans decrease, due to repayments and maturities. The yield on interest-earning assets decreased to 6.06% from 6.94%.

Interest Expense

Total interest expense for 2015 decreased 9.9% to \$69.2 million as compared to \$76.8 million for 2014. Such decrease reflects the lower cost of deposits (0.66% vs. 0.84%, before amortization adjustments). Such lower cost reflects continuing progress in the repricing of the Company's core retail deposits and other reductions in its cost of funds.

Net Interest Income

Net interest income for 2015 decreased to \$337.4 million when compared with \$408.5 million for 2014, mostly due to lower balances in our acquired loan portfolios and lower yields in our originated loan portfolio. The decrease also reflects a \$9.7 million decrease in interest income from loans to PREPA, which was placed in non-accrual at the end of the first quarter of 2015, and Puerto Rico Aqueducts and Sewer Authority ("PRASA"), which was paid off during the second quarter of 2015. Such decrease also reflects a decrease in net interest margin of 81 basis points to 5.03%.

Provision for Loan and Lease Losses

Provision for loan and lease losses increased \$100.9 million to \$161.5 million, reflecting \$32.9 million and \$5.2 million provision for loan and lease losses on non-performing acquired Eurobank and BBVAPR loans, respectively, as a result of the bulk sale of commercial NPAs during 2015. In addition, the Company recorded a \$53.3 million provision for loan and lease losses related to the PREPA line of credit, which was changed to non-accrual status during the first quarter of 2015.

Non-Interest Income

Core banking and wealth management revenues decreased 1.7% to \$76.6 million from \$77.9 million as compared to 2014, primarily reflecting a decrease of \$1.3 million and \$815 thousand in mortgage banking activities and wealth management revenue, respectively, and an increase of \$754 thousand in banking service revenue.

During 2015, the Company recognized an other-than-temporary impairment charge of \$1.5 million on its portfolio of investment securities available-for-sale classified as obligations from the Puerto Rico government and its political subdivisions. The Company determined that \$1.5 million of the unrealized loss carried by these securities was attributed to estimated credit losses.

The decrease in the FDIC shared-loss expense to \$42.8 million, compared to \$65.8 million in 2014, was principally driven by the expiration of the FDIC loss share coverage for commercial loans and other non-single family loans on June 30, 2015.

A \$20.0 million reimbursement from the FDIC was recognized in the statement of operations during 2015 related to the sale of a portion of covered non-performing commercial loans on September 28, 2015, as the FDIC agreed to cover \$20.0 million of losses as part of its loss-share agreement with the Company.

Non-Interest Expense

Non-interest expense of \$248.4 million, increased \$5.7 million or 2.3 % compared to 2014, primarily reflecting a \$9.3 million loss related to the bulk sale of non-performing acquired commercial loans, which included the sale of real estate owned with a carrying amount of \$11.0 million from the BBVAPR acquisition. Such increase also reflects an increase of \$2.8 million in electronic banking charges and \$1.5 million in legal fees related to PREPA's restructuring. The Company's efficiency ratio for 2015 was 60.00%, compared to 49.90% for 2014.

Income Tax Expense

Income tax benefit of \$17.6 million, primarily resulting from the 2015 loss, compared to an income tax expense of \$37.3 million in 2014.

Income Available to Common Shareholders

The Company's net loss to common shareholders amounted to \$16.4 million, compared to net income available to common shareholders of \$71.3 million for 2014. The loss per basic common share and fully diluted common share was \$0.37 for 2015, compared to income per basic common share of \$1.58 and fully diluted common share of \$1.50 for 2014.

Interest Earning Assets

The loan portfolio declined to \$4.434 billion at December 31, 2015, compared to \$4.827 billion at December 31, 2014, primarily due to the bulk sale of covered non-performing commercial loans with an unpaid principal balance amounting to \$197.1 million and the sale of non-performing commercial loans from the BBVAPR Acquisition with an unpaid principal balance amounting to \$38.1 million, as part of the same transaction, in addition to loan repayments and maturities as the Company continues to execute on its strategy to reduce its exposure to the Puerto Rico government. The investment portfolio of \$1.616 billion at December 31, 2015 increased 15.3% compared to \$1.402 billion at December 31, 2014.

Interest Bearing Liabilities

Total deposits amounted to \$4.717 billion at December 31, 2015, a decrease of 4.2% compared to \$4.924 billion at December 31, 2014. Interest bearing deposits decreased 5.3% to \$3.956 billion. Cost of deposits, which averaged 0.66% at December 31, 2014, decreased to 0.57% at December 31, 2015.

Stockholders' Equity

Stockholders' equity at December 31, 2015 was \$897.1 million compared to \$942.2 million at December 31, 2014, a decrease of 4.8%. This reflects a decrease of \$32.3 million in retained earnings and an increase of \$8.3 million in treasury stock. Book value per share was \$16.67 at December 31, 2015 compared to \$17.40 at December 31, 2014.

The Company maintains capital ratios in excess of regulatory requirements. At December 31, 2015, tier 1 leverage capital ratio was 11.18% (December 31, 2014 – 10.61%), tier 1 risk-based capital ratio was 15.99% (December 31, 2014 – 16.02%), and total risk-based capital ratio was 17.29% (December 31, 2014 – 17.57%). common equity tier 1 capital ratio under the new capital rules was 12.14% at December 31, 2015.

Return on Average Assets and Common Equity

Return on average common equity ("ROE") was (2.16%) compared to 9.50% for 2014. Return on average assets ("ROA") was (0.03%) compared to 1.10% for 2014. Both decreases reflect the net loss in 2015.

Assets under Management

At December 31, 2015, total assets managed by the Company's trust division and OPC decreased to \$2.691 billion compared to \$2.841 billion at December 31, 2014. At December 31, 2015, total assets gathered by the securities broker-dealer subsidiary from its customer investment accounts decreased to \$2.375 billion, compared to \$2.622 billion at December 31, 2014. Changes in trust and broker-dealer related assets primarily reflect a decrease in portfolio balances and fluctuations in market values.

Lending

Total loan production of \$1.014 billion increased by 10.3% compared to 2014. Total commercial loan production of \$365.2 million increased by 38.9% from \$262.9 million for 2014, mostly from corporate and institutional loans. Mortgage loan production of \$247.2 million increased by 14.8% from \$215.4 million. In the aggregate, consumer loan and auto and leasing production totaled \$401.5 million, an increase of 9.0% from 2014.

Credit Quality on Non-Acquired Loans

Net credit losses, excluding acquired loans, increased \$9.1 million to \$38.1 million, representing 1.30% of average non-acquired loans outstanding versus 1.11% in 2014. The allowance for loan and lease losses, excluding acquired loans, at December 31, 2015, increased to \$112.6 million (3.62% of total non-acquired loans) compared to \$51.4 million (1.81% of total non-acquired loans) at December 31, 2014, mostly from the PREPA allowance of \$53.3 million in 2015.

Non-GAAP Measures

The Company uses certain non-GAAP measures of financial performance to supplement the consolidated financial statements presented in accordance with GAAP. The Company presents non-GAAP measures that management believes are useful and

meaningful to investors. Non-GAAP measures do not have any standardized meaning, are not required to be uniformly applied, and are not audited. Therefore, they are unlikely to be comparable to similar measures presented by other companies. The presentation of non-GAAP measures is not intended to be a substitute for, and should not be considered in isolation from, the financial measures reported in accordance with GAAP.

The Company's management has reported and discussed the results of operations herein both on a GAAP basis and on a pre-tax pre-provision operating income basis (defined as net interest income, plus banking and financial services revenue, less non-interest expenses, as calculated in the table below). The Company's management believes that, given the nature of the items excluded from the definition of pre-tax pre-provision operating income, it is useful to state what the results of operations would have been without them so that investors can see the financial trends from the Company's continuing business.

During the year ended December 31, 2015, the Company's pre-tax pre-provision operating income decreased 32.0% to \$165.6 million as compared to \$243.7 million for 2014. Pre-tax pre-provision operating income is calculated as follows:

	Year Ended December 31,		
	2015	2014	2013
	(In thousands)		
<u>PRE-TAX PRE-PROVISION OPERATING INCOME</u>			
Net interest income	\$ 337,372	\$ 408,475	\$ 409,672
Core non-interest income:			
Banking service revenue	41,466	40,712	44,239
Wealth management revenue	29,040	29,855	30,924
Mortgage banking activities	6,128	7,381	10,994
Total core non-interest income	76,634	77,948	86,157
Non-interest expenses	248,401	242,725	264,136
Less merger and restructuring charges	-	-	(17,660)
Total pre-tax pre-provision operating income	\$ 165,605	\$ 243,698	\$ 249,353

Tangible common equity consists of common equity less goodwill, core deposit intangibles and customer relationship intangible. Tangible book value per common share consists of tangible common equity divided by common stock outstanding at the end of the period. Ratios of tangible common equity to total assets, tangible common equity to risk-weighted assets, total equity to risk-weighted assets, tier 1 common equity to risk-weighted assets, and tangible book value per common share are non-GAAP measures and are not codified in the federal banking regulations.

At December 31, 2015, tangible common equity to total assets decreased to 8.98% from 9.14% and tangible common equity to risk-weighted assets decreased to 13.02% from 14.04% at December 31, 2014. Total equity to risk-weighted assets decreased to 18.32% from 19.44% at December 31, 2014.

Management and many stock analysts use tangible common equity in conjunction with more traditional bank capital ratios to compare the capital adequacy of banking organizations. Tangible common equity or related measures should not be considered in isolation or as a substitute for stockholders' equity, total assets or any other measure calculated in accordance with GAAP.

ANALYSIS OF RESULTS OF OPERATIONS

The following tables show major categories of interest-earning assets and interest-bearing liabilities, their respective interest income, expenses, yields and costs, and their impact on net interest income due to changes in volume and rates for the years ended 2015 and 2014:

TABLE 1 - YEAR-TO-DATE ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

	Interest		Average rate		Average balance	
	December 2015	December 2014	December 2015	December 2014	December 2015	December 2014
	(Dollars in thousands)					
A - TAX EQUIVALENT SPREAD						
Interest-earning assets	\$ 406,568	\$ 485,257	6.06%	6.94%	\$ 6,704,995	\$ 6,992,631
Tax equivalent adjustment	6,891	50,793	0.10%	0.73%	-	-
Interest-earning assets - tax equivalent	413,459	536,050	6.16%	7.67%	6,704,995	6,992,631
Interest-bearing liabilities	69,196	76,782	1.11%	1.15%	6,226,372	6,663,591
Tax equivalent net interest income / spread	344,263	459,268	5.05%	6.52%	478,623	329,040
Tax equivalent interest rate margin			5.13%	6.57%		
B - NORMAL SPREAD						
Interest-earning assets:						
Investments:						
Investment securities	37,596	48,242	2.49%	3.33%	1,508,819	1,450,778
Trading securities	70	151	8.25%	8.67%	848	1,741
Interest bearing cash and money market investments	1,280	1,311	0.26%	0.23%	491,051	573,403
Total investments	38,946	49,704	1.95%	2.45%	2,000,718	2,025,922
Non-acquired loans						
Mortgage	39,778	40,978	5.16%	5.21%	771,322	786,607
Commercial	60,931	64,328	4.56%	5.41%	1,336,510	1,190,038
Consumer	21,003	15,367	10.35%	10.04%	202,971	153,067
Auto and leasing	62,108	51,971	9.86%	10.38%	629,910	500,720
Total non-acquired loans	183,820	172,644	6.25%	6.56%	2,940,713	2,630,432
Acquired loans:						
Acquired BBVAPR						
Mortgage	34,842	37,612	5.55%	5.46%	628,340	689,408
Commercial	48,730	73,403	10.65%	11.29%	457,767	649,936
Consumer	13,187	15,412	16.35%	13.70%	80,666	112,477
Auto	34,633	47,513	9.03%	8.62%	383,583	551,186
Total acquired BBVAPR loans	131,392	173,940	8.47%	8.68%	1,550,356	2,003,007
Acquired Eurobank	52,410	88,969	24.58%	26.70%	213,208	333,270
Total loans	367,622	435,553	7.81%	8.77%	4,704,277	4,966,709
Total interest earning assets	406,568	485,257	6.06%	6.94%	6,704,995	6,992,631

	Interest		Average rate		Average balance	
	December 2015	December 2014	December 2015	December 2014	December 2015	December 2014
(Dollars in thousands)						
Interest-bearing liabilities:						
Deposits:						
NOW Accounts	4,451	8,001	0.38%	0.56%	1,163,424	1,417,272
Savings and money market	6,504	8,097	0.52%	0.69%	1,256,909	1,169,482
Individual retirement accounts	2,482	3,760	0.88%	1.15%	281,197	325,678
Retail certificates of deposits	5,397	6,852	1.32%	1.39%	409,038	491,485
Total core deposits	18,834	26,710	0.61%	0.78%	3,110,568	3,403,917
Institutional deposits	2,790	4,961	1.04%	1.42%	268,678	348,742
Brokered deposits	4,900	5,715	0.78%	0.82%	624,210	697,756
Total wholesale deposits	7,690	10,676	0.86%	1.02%	892,888	1,046,498
	26,524	37,386	0.66%	0.84%	4,003,456	4,450,415
Non-interest bearing deposits	-	-	0.00%	0.00%	769,790	715,729
Deposits fair value premium amortization	(660)	(4,773)	0.00%	0.00%	-	-
Core deposit intangible amortization	1,170	1,341	0.00%	0.00%	-	-
Total deposits	27,034	33,954	0.57%	0.66%	4,773,246	5,166,144
Borrowings:						
Securities sold under agreements to repurchase	29,567	29,654	2.92%	2.85%	1,012,756	1,041,378
Advances from FHLB and other borrowings	9,072	9,185	2.68%	2.58%	338,299	355,322
Subordinated capital notes	3,523	3,989	3.45%	3.96%	102,071	100,747
Total borrowings	42,162	42,828	2.90%	2.86%	1,453,126	1,497,447
Total interest bearing liabilities	69,196	76,782	1.11%	1.15%	6,226,372	6,663,591
Net interest income / spread	\$ 337,372	\$ 408,475	4.95%	5.79%		
Interest rate margin			5.03%	5.84%		
Excess of average interest-earning assets					\$ 478,623	\$ 329,040
over average interest-bearing liabilities						
Average interest-earning assets to average					107.69%	104.94%
interest-bearing liabilities ratio						

C - CHANGES IN NET INTEREST INCOME DUE TO:

	Volume	Rate	Total
	(In thousands)		
Interest Income:			
Investments	\$ (729)	\$ (10,029)	\$ (10,758)
Loans	(42,700)	(25,231)	(67,931)
Total interest income	(43,429)	(35,260)	(78,689)
Interest Expense:			
Deposits	(2,582)	(4,338)	(6,920)
Repurchase agreements	(815)	728	(87)
Other borrowings	(453)	(126)	(579)
Total interest expense	(3,850)	(3,736)	(7,586)
Net Interest Income	\$ (39,579)	\$ (31,524)	\$ (71,103)

TABLE 1A - YEAR-TO-DATE ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

	Interest		Average rate		Average balance	
	December 2014	December 2013	December 2014	December 2013	December 2014	December 2013
	(Dollars in thousands)					
A - TAX EQUIVALENT SPREAD						
Interest-earning assets	\$ 485,257	\$ 493,632	6.94%	6.58%	\$ 6,992,631	\$ 7,499,993
Tax equivalent adjustment	50,793	41,106	0.73%	0.55%	-	-
Interest-earning assets - tax equivalent	536,050	534,738	7.67%	7.13%	6,992,631	7,499,993
Interest-bearing liabilities	76,782	83,960	1.15%	1.12%	6,663,591	7,482,019
Tax equivalent net interest income / spread	459,268	450,778	6.52%	6.01%	329,040	17,974
Tax equivalent interest rate margin			6.57%	6.01%		
B - NORMAL SPREAD						
Interest-earning assets:						
Investments:						
Investment securities	48,242	48,456	3.33%	2.60%	1,450,778	1,862,274
Trading securities	151	117	8.67%	6.56%	1,741	1,784
Interest bearing cash and money market investments	1,311	1,157	0.23%	0.21%	573,403	540,724
Total investments	49,704	49,730	2.45%	2.07%	2,025,922	2,404,782
Non-acquired loans						
Mortgage	40,978	43,531	5.21%	5.71%	786,607	762,403
Commercial	64,328	32,891	5.41%	4.95%	1,190,038	663,968
Consumer	15,367	8,058	10.04%	9.34%	153,067	86,250
Auto and leasing	51,971	21,181	10.38%	9.94%	500,720	213,127
Total non-acquired loans	172,644	105,661	6.56%	6.12%	2,630,432	1,725,748
Acquired loans:						
Acquired BBVAPR						
Mortgage	37,612	42,740	5.46%	5.60%	689,408	763,195
Commercial	73,403	114,492	11.29%	9.38%	649,936	1,220,471
Consumer	15,412	21,147	13.70%	13.13%	112,477	161,120
Auto	47,513	68,093	8.62%	7.99%	551,186	852,165
Total acquired BBVAPR loans	173,940	246,472	8.68%	8.22%	2,003,007	2,996,951
Acquired Eurobank	88,969	91,769	26.70%	24.64%	333,270	372,512
Total loans	435,553	443,902	8.77%	8.71%	4,966,709	5,095,211
Total interest earning assets	485,257	493,632	6.94%	6.58%	6,992,631	7,499,993

	Interest		Average rate		Average balance	
	December 2014	December 2013	December 2014	December 2013	December 2014	December 2013
			(Dollars in thousands)			
Interest-bearing liabilities:						
Deposits:						
NOW Accounts	\$ 8,001	\$ 11,151	0.56%	0.77%	\$ 1,417,272	\$ 1,452,030
Savings and money market	8,097	9,481	0.69%	1.01%	1,169,482	938,450
Individual retirement accounts	3,760	4,832	1.15%	1.35%	325,678	358,605
Retail certificates of deposits	6,852	11,203	1.39%	1.66%	491,485	674,241
Total core deposits	26,710	36,667	0.78%	1.07%	3,403,917	3,423,326
Institutional deposits	4,961	9,983	1.42%	1.66%	348,742	602,769
Brokered deposits	5,715	7,068	0.82%	0.86%	697,756	821,112
Total wholesale deposits	10,676	17,051	1.02%	1.20%	1,046,498	1,423,881
	37,386	53,718	0.84%	1.11%	4,450,415	4,847,207
Non-interest bearing deposits	-	-	0.00%	0.00%	715,729	\$ 751,757
Deposits fair value premium amortization	(4,773)	(14,400)	0.00%	0.00%	-	-
Core deposit intangible amortization	1,341	1,659	0.00%	0.00%	-	-
Total deposits	33,954	40,977	0.66%	0.73%	5,166,144	5,598,964
Borrowings:						
Securities sold under agreements to repurchase	29,654	29,249	2.85%	2.16%	1,041,378	1,353,011
Advances from FHLB and other borrowings	9,185	8,620	2.58%	2.05%	355,322	419,880
Subordinated capital notes	3,989	5,114	3.96%	4.64%	100,747	110,164
Total borrowings	42,828	42,983	2.86%	2.28%	1,497,447	1,883,055
Total interest bearing liabilities	76,782	83,960	1.15%	1.12%	6,663,591	7,482,019
Net interest income / spread	\$ 408,475	\$ 409,672	5.79%	5.46%		
Interest rate margin			5.84%	5.46%		
Excess of average interest-earning assets over					\$ 329,040	\$ 17,974
average interest-bearing liabilities						
Average interest-earning assets to average					104.94%	100.24%
interest-bearing liabilities ratio						

C - CHANGES IN NET INTEREST INCOME DUE TO:

	Volume	Rate	Total
	(In thousands)		
Interest Income:			
Investments	\$ (7,835)	\$ 7,809	\$ (26)
Loans	(16,322)	7,973	(8,349)
Total interest income	(24,157)	15,782	(8,375)
Interest Expense:			
Deposits	(3,168)	(3,855)	(7,023)
Repurchase agreements	(6,737)	7,142	405
Other borrowings	(1,917)	1,357	(560)
Total interest expense	(11,822)	4,644	(7,178)
Net Interest Income	\$ (12,335)	\$ 11,138	\$ (1,197)

Net Interest Income

Comparison for the years ended December 31, 2015 and 2014

Net interest income is a function of the difference between rates earned on the Company's interest-earning assets and rates paid on its interest-bearing liabilities (interest rate spread) and the relative amounts of its interest earning assets and interest-bearing liabilities (interest rate margin). The Company constantly monitors the composition and re-pricing of its assets and liabilities to maintain its net interest income at adequate levels. Table 1 above shows the major categories of interest-earning assets and interest-bearing liabilities, their respective interest income, expenses, yields and costs, and their impact on net interest income due to changes in volume and rates for 2015 and 2014.

Net interest income of \$337.4 million decreased 17.4% compared with \$408.5 million reported in 2014, reflecting a decrease of 15.6% in interest income from loans and a decrease of 21.6% in interest income from investments.

Interest rate spread decreased 84 basis points from 5.79% to 4.95%. This decrease is mainly due to the net effect of a 88 basis points decrease in the average yield of interest-earning assets from 6.94% to 6.06%, reflecting reduction in high yielding loan portfolios including Puerto Rico government credit and acquired loan portfolio.

Interest income decreased to \$406.6 million from \$485.3 million in 2014. Such decrease reflects decreases of \$43.4 million and \$35.3 million in the volume and interest rate, respectively, of interest-earning assets. Interest income from loans decreased 15.6% to \$367.6 million, reflecting a decrease in both, volume and interest rate of \$42.7 million and \$25.2 million, respectively. Such decrease reflects lower acquired loan balances and yield mainly related to the bulk sale at the end of the third quarter of 2015 and also normal repayments and maturities. In addition, the decrease reflects a \$9.7 million decrease in interest income from loans to PREPA, which was placed in non-accrual status at the end of the first quarter of 2015, and Puerto Rico Aqueducts and Sewer Authority ("PRASA"), which was paid off during the second quarter of 2015. Non-acquired loans interest income increased 6.5% to \$183.8 million as average balances grew 11.8% and yield contracted 31 basis points to 6.25%. Acquired BBVAPR loans interest income fell 24.5% to \$131.4 million as average balances declined 22.6% and yield decreased 21 basis points to 8.47%. Acquired Eurobank loans interest income fell 41.1% to \$52.4 million as average balances declined 36.0% and yield decreased 212 basis points to 24.58%. Interest income from investments decreased 21.6% to \$38.9 million, reflecting a decrease in interest rate and volume of \$10.0 million and \$729 thousand, respectively. Such decrease in interest income from investments reflects a decrease in investment securities from redemptions, maturities and sales, and higher premium amortization on existing securities.

Interest expense decreased 9.9% to \$69.2 million, primarily because of a \$3.9 million decrease in the volume of interest-bearing liabilities and a decrease of \$3.7 million in interest rate. The decrease in interest-bearing liabilities is mostly due to the decrease of \$2.6 million in deposits volume and \$4.3 million in interest rate, a decrease of \$815

thousand in repurchase agreements volume which was partially offset by an increase of \$728 thousand in interest rate, and a decrease in other borrowings volume of \$453 thousand and \$126 thousand in interest rate. The cost of interest bearing deposits before fair value amortization and core deposit intangible amortization decreased 18 basis points to 0.66%, compared to 0.84% for 2014. The decrease in the cost of deposits was partially offset by an increase in the cost of borrowings, which increased 4 basis points to 2.90% from 2.86%.

The average balance of total interest-earning assets was \$6.704 billion, a decrease of 4.1% from 2014. The decrease in average balance of interest-earning assets was mainly attributable to a decrease of 1.2% in average investments and a decrease of 5.3% in average loans.

Comparison of years ended December 31, 2014 and 2013

Net interest income amounted to \$408.5 million, a slight decrease of 0.3% from \$409.7 million for 2013. This change reflects a decrease of 1.8% in interest income from loans and a 17.1% decrease in interest expense from deposits, when comparing the years 2014 and 2013.

Interest rate spread for 2014 increased 33 basis points to 5.79% from 5.46% in 2013. This increase is mainly due to the net effect of a 36 basis point increase in the average yield of interest-earning assets from 6.58% to 6.94%, and a 3 basis point increase in the average cost of funds from 1.12% to 1.15%.

Interest income for 2014 decreased to \$485.3 million from \$493.6 million in 2013. Such decrease reflects \$24.2 million reduction in the volume of interest-earning assets, partially offset by an increase in rate of \$15.8 million. Interest income from loans decreased 1.9% to \$435.6 million, primarily reflecting a decrease in volume of \$16.3 million, partially offset by an \$8.0 million increase in interest rate. Interest income from investments remained leveled at \$49.7 million compared to 2013, reflecting a decrease in volume of \$7.8 million, offset by a \$7.8 million increase in interest rate.

Interest expense for 2014 decreased 8.5% to \$76.8 million from \$84.0 million in 2013. The decrease was primarily the net result of an \$11.8 million decrease in the volume of interest-bearing liabilities and an increase of \$4.6 million in interest rate. The decrease in interest-bearing liabilities was mostly due to the decrease in repurchase agreements volume of \$6.7 million, and a decrease in deposits volume of \$3.2 million and deposits interest rate of \$3.9 million, partially offset by a \$7.1 million increase in repurchase agreements interest rate. The cost of interest bearing deposits before fair value amortization and core deposit intangible amortization decreased 27 basis points to 0.84% for 2014, compared to 1.11% for 2013. The decrease in the cost of deposits was partially offset by an increase in the cost of borrowings, which increased 58 basis points to 2.86% from 2.28%.

For 2014, the average balance of total interest-earning assets was \$6.993 billion, a decrease of \$507.4 million, or 6.8%, from 2013. Such decrease was mainly attributable to a decline of \$378.9 million, or 22.1%, in average investment securities, resulting from sales, redemptions and maturities during 2014. The average yield on interest-earning assets was 6.94% compared to 6.58% for 2013. The yield of the investment portfolio increased to 2.45% from 2.07%. Increase in investment yield is related to lower premium amortization in the mortgage-backed securities portfolio from the extension of the duration of the portfolio as a result of the level of market rates.

TABLE 2 - NON-INTEREST INCOME SUMMARY

	Year Ended December 31,			
	2015	2014	Variance	2013
	(Dollars in thousands)			
Banking service revenue	\$ 41,466	\$ 40,712	1.9%	\$ 44,239
Wealth management revenue	29,040	29,855	-2.7%	30,924
Mortgage banking activities	6,128	7,381	-17.0%	10,994
Total banking and financial service revenue	76,634	77,948	-1.7%	86,157
Total other-than-temporary impairment losses on investment securities	(4,662)	-	-100.0%	-
Portion of loss recognized in other comprehensive income, before taxes	3,172	-	100.0%	-
Net impairment losses recognized in earnings	(1,490)	-	-100.0%	-
FDIC shared-loss expense, net:				
FDIC indemnification asset expense	(40,131)	(62,285)	35.6%	(66,253)
Change in true-up payment obligation	(2,677)	(3,471)	22.9%	(3,014)
	(42,808)	(65,756)	34.9%	(69,267)
Reimbursement from FDIC shared-loss coverage in sale of loans	20,000	-	100.0%	-
Net gain (loss) on:				

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Sale of securities available for sale	2,572	4,366	-41.1%	-
Derivatives	(190)	(608)	68.8%	(1,526)
Early extinguishment of debt	-	-	0.0%	1,061
Other non-interest (loss) income	(2,246)	1,373	-263.6%	670
	(24,162)	(60,625)	60.1%	(69,062)
Total non-interest income, net	\$ 52,472	\$ 17,323	202.9%	\$ 17,095

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Non-Interest Income

Non-interest income is affected by the level of trust assets under management, transactions generated by clients' financial assets serviced by the securities broker-dealer and insurance agency subsidiaries, the level of mortgage banking activities, and the fees generated from loans and deposit accounts. It is also affected by the FDIC shared-loss expense, which varies depending on the results of the on-going evaluation of expected cash flows of the loan portfolio acquired in the FDIC-assisted acquisition. In addition, it is affected by the amount of securities, derivatives, trading and other transactions.

Comparison of years ended December 31, 2015 and 2014

As shown in Table 2 above, the Company recorded non-interest income in the amount of \$52.5 million, compared to \$17.3 million for 2014, an increase of 202.9%, or \$35.2 million, mostly from a \$20.0 million reimbursement from the FDIC upon successful negotiation and termination of the commercial shared-loss coverage.

The net FDIC shared-loss expense decreased to \$42.8 million as compared to \$65.8 million for 2014, primarily from the decrease of the FDIC commercial loss share amortization related to the expiration of the non-single family loss share coverage by the FDIC. The decrease is also related to the ongoing evaluation of expected cash flows of the covered loan portfolio and from changes in the fair value of the true-up payment obligation (also known as a clawback liability). The FDIC indemnification asset expense decreased to \$40.1 million from \$62.3 million compared with 2014. The true-up payment obligation decreased to \$2.7 million as compared to \$3.5 million for 2014. The true-up payment obligation may increase if actual and expected losses decline. The Company measures the true-up payment obligation at fair value. Notwithstanding the expiration of loss share coverage for non-single family loans, on July 2, 2015, the Company entered into an agreement with the FDIC pursuant to which the FDIC concurred with a sale of loss-share assets covered under the non-single family loss share agreement. As a result to such agreement, the FDIC agreed and paid \$20 million in loss share coverage with respect to the aggregate loss resulting from the recent bulk sale of covered non-performing commercial loans, as reflected in Table 2, and such reimbursement was received in December 2015.

Banking service revenue, which consists primarily of fees generated by deposit accounts, electronic banking services, and customer services, increased to \$41.5 million, from \$40.7 million for 2014. The increase is mainly driven by higher electronic banking fees of \$2.4 million, partially offset by lower checking account fees by \$1.4 million.

Wealth management revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, decreased to \$29.0 million from \$29.9 million in 2014, mainly due to a decrease in mutual fund and over-the-counter trading of \$680 thousand and lower bond sales by \$294 thousand.

Income generated from mortgage banking activities decreased 17.0% to \$6.1 million, compared to \$7.4 million 2014. The decrease in mortgage banking activities was mostly due to foregone gains on sales as a result of retaining securitized GNMA pools. The Company retained securitized GNMA pools totaling \$54.5 million at a yield of 3.09% from its own originations during the second half of 2015.

During 2015, the Company recognized an other-than-temporary impairment charge on its portfolio of investment securities available-for-sale classified as obligations from the Puerto Rico government and its political subdivisions. The Corporation determined that \$1.5 million of the unrealized loss carried by these securities was attributed to estimated credit losses.

Gains from the sale of securities were \$2.6 million compared to \$4.4 million for the same period in 2014. Losses from derivative activities were \$190 thousand, compared to \$608 thousand for 2014.

Other non-interest income declined \$3.6 million, mainly related to the sale during the second quarter of 2015 of GNMA mortgage loan servicing rights for approximately \$7.0 million. The Company recognized a loss of \$2.7 million related to this transaction.