OFG BANCORP
Form 10-Q
August 09, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2013

or

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

For the transition period from ______________ to ______________

Commission File Number 001-12647

OFG Bancorp

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

Principal Executive Offices:

254 Muñoz Rivera Avenue

San Juan, Puerto Rico 00918

Telephone Number: (787) 771-6800

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

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

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

Large Accelerated Filer ¨ Accelerated Filer x Non-Accelerated Filer ¨ Smaller Reporting Company ¨
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

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

45,640,105 common shares ($1.00 par value per share) outstanding as of July 31, 2013

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FORWARD-LOOKING STATEMENTS

The information included in this quarterly report on Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements may relate to the financial condition, results of operations, plans, objectives, future performance and business of OFG Bancorp, formerly known as Oriental Financial Group Inc. ("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 a "will," "would," "should," "could," "might," "can," "may," or similar expressions are generally intended to identify forward-lo 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:

- the rate of growth in the economy and employment levels, as well as general business and economic conditions;
- changes in interest rates, as well as the magnitude of such changes;
- the fiscal and monetary policies of the federal government and its agencies;
- a credit default by the U.S. or Puerto Rico governments or a downgrade in the credit ratings of the U.S. or Puerto Rico governments;
- changes in federal bank regulatory and supervisory policies, including required levels of capital;
- the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") on the Company's businesses, business practices and cost of operations;
- the relative strength or weakness of the consumer and commercial credit sectors and of the real estate market in Puerto Rico;
- the performance of the stock and bond markets;
- competition in the financial services industry;
- additional Federal Deposit Insurance Corporation ("FDIC") assessments;

- possible legislative, tax or regulatory changes; and

- difficulties in integrating the acquired Puerto Rico operations of Banco Bilbao Vizcaya Argentaria, S. A. ("BBVAPR") into the Company's operations.

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

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

Item 1. Financial Statements

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

AS OF JUNE 30, 2013 AND DECEMBER 31, 2012

	June 30, 2013	December 31, 2012
	(In thousands, except share data)	
ASSETS		
Cash and cash equivalents		
Cash and due from banks	$ 737,330	$ 855,490
Money market investments	10,983	13,205
Total cash and cash equivalents	**748,313**	**868,695**
Securities purchased under agreements to resell	**-**	**80,000**
Investments:		
Trading securities, at fair value, with amortized cost of $2,286 (December 31, 2012 - $508)	2,209	495
Investment securities available-for-sale, at fair value, with amortized cost of $1,807,335 (December 31, 2012 - $2,118,825)	1,836,229	2,194,286
Federal Home Loan Bank (FHLB) stock, at cost	22,156	38,411
Other investments	66	73
Total investments	**1,860,660**	**2,233,265**
Securities sold but not yet delivered	**16,732**	**-**
Loans:		
Mortgage loans held-for-sale, at lower of cost or fair value	78,350	64,145
Loans not covered under shared-loss agreements with the FDIC, net of allowance for loan and lease losses of $46,625 (December 31, 2012 - $39,921)	4,543,299	4,709,778
Loans covered under shared-loss agreements with the FDIC, net of allowance for loan and lease losses of $53,992 (December 31, 2012 - $54,124)	369,380	395,307
Total loans, net	**4,991,029**	**5,169,230**
Other assets:		
FDIC shared-loss indemnification asset	236,472	286,799
Foreclosed real estate covered under shared-loss agreements with the FDIC	25,193	22,283
Foreclosed real estate not covered under shared-loss agreements with the FDIC	56,496	51,233
Accrued interest receivable	17,508	17,554
Deferred tax asset, net	155,165	122,501
Premises and equipment, net	84,301	84,997
Customers' liability on acceptances	30,571	26,996
Servicing assets	12,994	10,795
Derivative assets	19,655	21,889
Goodwill	76,383	76,383

Other assets		104,462		123,642
Total assets	$	**8,435,934**	$	**9,196,262**
LIABILITIES AND STOCKHOLDERS' EQUITY				
Deposits:				
Demand deposits	$	2,294,635	$	2,447,152
Savings accounts		1,006,558		634,819
Certificates of deposit		2,363,845		2,607,588
Total deposits		**5,665,038**		**5,689,559**
Borrowings:				
Short term borrowings		-		92,210
Securities sold under agreements to repurchase		1,313,870		1,695,247
Advances from FHLB and other borrowings		322,300		554,177
Subordinated capital notes		98,961		146,038
Total borrowings		**1,735,131**		**2,487,672**
Other liabilities:				
Derivative liabilities		16,701		26,260
Acceptances executed and outstanding		30,571		26,996
Accrued expenses and other liabilities		117,569		102,169
Total liabilities		**7,565,010**		**8,332,656**
Commitments and contingencies (See Notes 14 and 15)				
Stockholders' equity:				
Preferred stock; 10,000,000 shares authorized; 1,340,000 shares of Series A, 1,380,000 shares of Series B, and 960,000 shares of Series D issued and outstanding, (December 31, 2012 - 1,340,000; 1,380,000; and 960,000) $25 liquidation value		92,000		92,000
84,000 shares of Series C issued and outstanding (December 31, 2012 - 84,000); $1,000 liquidation value		84,000		84,000
Common stock, $1 par value; 100,000,000 shares authorized; 52,688,584 shares issued; 45,640,105 shares outstanding (December 31, 2012 - 52,670,878; 45,580,281)		52,689		52,671
Additional paid-in capital		538,105		537,453
Legal surplus		57,906		52,143
Retained earnings		111,292		70,734
Treasury stock, at cost, 7,048,479 shares (December 31, 2012 - 7,090,597 shares)		(80,834)		(81,275)
Accumulated other comprehensive income, net of tax of -$174 (December 31, 2012 - $1,802)		15,766		55,880
Total stockholders' equity		**870,924**		**863,606**
Total liabilities and stockholders' equity	$	**8,435,934**	$	**9,196,262**

See notes to unaudited consolidated financial statements.

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UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE QUARTERS AND SIX-MONTH PERIODS ENDED JUNE 30, 2013 AND 2012

	Quarter Ended June 30, 2013	Quarter Ended June 30, 2012	Six-Month Period Ended June 30, 2013	Six-Month Period Ended June 30, 2012
	(In thousands, except per share data)			
Interest income:				
Loans not covered under shared-loss agreements with the FDIC	$ 90,611	$ 17,223	$ 170,874	$ 35,345
Loans covered under shared-loss agreements with the FDIC	23,999	20,342	44,228	41,884
Total interest income from loans	**114,610**	**37,565**	**215,102**	**77,229**
Mortgage-backed securities	9,080	21,573	19,898	49,636
Investment securities and other	2,118	1,650	4,436	3,843
Total interest income	**125,808**	**60,788**	**239,436**	**130,708**
Interest expense:				
Deposits	9,973	7,885	20,451	17,008
Securities sold under agreements to repurchase	7,109	16,500	14,357	34,070
Advances from FHLB and other borrowings	2,187	2,926	3,847	5,930
FDIC-guaranteed term notes	-	-	-	909
Subordinated capital notes	1,170	321	2,830	649
Total interest expense	**20,439**	**27,632**	**41,485**	**58,566**
Net interest income	**105,369**	**33,156**	**197,951**	**72,142**
Provision for non-covered loan and lease losses	37,527	3,800	45,443	6,800
Provision for covered loan and lease losses, net	1,211	1,467	1,883	8,624
Total provision for loan and lease losses	**38,738**	**5,267**	**47,326**	**15,424**
Net interest income after provision for loan and lease losses	**66,631**	**27,889**	**150,625**	**56,718**
Non-interest income:				
Financial service revenue	8,030	5,903	15,690	11,791
Banking service revenue	13,334	3,145	25,716	6,225
Mortgage banking activities	2,525	2,436	5,679	4,938
Total banking and financial service revenues	**23,889**	**11,484**	**47,085**	**22,954**
FDIC shared-loss expense, net	(19,965)	(5,583)	(32,836)	(10,410)
Net gain (loss) on:				
Sale of securities	-	11,979	-	19,338
Derivatives	1,569	(107)	1,271	(108)
Early extinguishment of subordinated capital notes	-	-	1,061	-

Other	2,303	63	2,349	(779)
Total non-interest income, net	**7,796**	**17,836**	**18,930**	**30,995**
Non-interest expense:				
Compensation and employee benefits	24,089	11,184	47,338	21,550
Professional and service fees	7,710	5,222	16,832	10,643
Occupancy and equipment	8,066	4,292	17,282	8,501
Insurance	2,723	1,442	5,401	3,262
Electronic banking charges	4,094	1,609	7,822	3,166
Advertising, business promotion, and strategic initiatives	1,670	1,564	3,079	2,412
Merger and restructuring charges	5,274	-	10,808	-
Foreclosure, repossession and other real estate expenses	2,156	936	3,661	1,686
Loan servicing and clearing expenses	1,884	955	3,360	1,923
Taxes, other than payroll and income taxes	5,132	(107)	7,754	1,067
Loss on sale of foreclosed real estate and other repossessed assets	1,696	886	3,573	1,282
Communication	835	392	1,699	781
Printing, postage, stationary and supplies	851	322	2,017	630
Director and investor relations	377	342	613	651
Other	2,265	671	4,393	1,555
Total non-interest expense	**68,822**	**29,710**	**135,632**	**59,109**
Income before income taxes	**5,605**	**16,015**	**33,923**	**28,604**
Income tax expense (benefit)	(31,934)	1,057	(24,808)	2,994
Net income	**37,539**	**14,958**	**58,731**	**25,610**
Less: dividends on preferred stock	(3,466)	(1,201)	(6,931)	(2,401)
Income available to common shareholders	**$ 34,073**	**$ 13,757**	**$ 51,800**	**$ 23,209**
Earnings per common share:				
Basic	**$ 0.75**	**$ 0.34**	$ **1.14**	**$ 0.57**
Diluted	**$ 0.68**	**$ 0.34**	$ **1.05**	**$ 0.57**
Average common shares outstanding and equivalents	**52,968**	**40,808**	**52,929**	**40,986**
Cash dividends per share of common stock	**$ 0.06**	**$ 0.06**	$ **0.12**	**$ 0.12**

See notes to unaudited consolidated financial statements.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE QUARTERS AND SIX-MONTHS PERIODS ENDED JUNE 30, 2013 AND 2012

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
Net income	**$ 37,539**	**$ 14,958**	**$ 58,731**	**$ 25,610**
Other comprehensive loss before tax:				
Unrealized (gain) loss on securities available-for-sale	(35,576)	7,059	(46,568)	9,000
Realized gain on investment securities included in net income	-	(11,979)	-	(19,338)
Unrealized loss (gain) on cash flow hedges	3,016	(6,791)	4,477	(8,792)
Other comprehensive loss before taxes	**(32,560)**	**(11,711)**	**(42,091)**	**(19,130)**
Income tax effect	1,275	2,875	1,977	3,260
Other comprehensive loss after taxes	**(31,285)**	**(8,836)**	**(40,114)**	**(15,870)**
Comprehensive income	**$ 6,254**	**$ 6,122**	**$ 18,617**	**$ 9,740**

See notes to unaudited consolidated financial statements.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2013 AND 2012

	Six-Month Period Ended June 30, 2013	2012
	(In thousands)	
Preferred stock:		
Balance at beginning and end of period	**$ 176,000**	**$ 68,000**
Common stock:		
Balance at beginning of year	52,671	47,809
Exercised stock options	18	33
Balance at end of period	**52,689**	**47,842**
Additional paid-in capital:		
Balance at beginning of year	537,453	499,096
Stock-based compensation expense	888	787
Exercised stock options	167	361
Lapsed restricted stock units	(364)	(392)
Common stock issuance costs	(16)	-
Preferred stock issuance costs	(23)	-
Balance at end of period	**538,105**	**499,852**
Legal surplus:		
Balance at beginning of year	52,143	50,178
Transfer from retained earnings	5,763	2,490
Balance at end of period	**57,906**	**52,668**
Retained earnings:		
Balance at beginning of year	70,734	68,149
Net income	58,731	25,610
Cash dividends declared on common stock	(5,479)	(4,886)
Cash dividends declared on preferred stock	(6,931)	(2,401)
Transfer to legal surplus	(5,763)	(2,490)
Balance at end of period	**111,292**	**83,982**
Treasury stock:		
Balance at beginning of year	(81,275)	(74,808)
Stock repurchased	-	(7,022)
Lapsed restricted stock units	364	392
Stock used to match defined contribution plan	77	35
Balance at end of period	**(80,834)**	**(81,403)**
Accumulated other comprehensive income, net of tax:		
Balance at beginning of year	55,880	37,131
Other comprehensive loss, net of tax	(40,114)	(15,870)
Balance at end of period	**15,766**	**21,261**
Total stockholders' equity	**$ 870,924**	**$ 692,202**

See notes to unaudited consolidated financial statements.

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2013 AND 2012

	Six-Month Period Ended June 30, 2013	2012
	(In thousands)	
Cash flows from operating activities:		
Net income	$ **58,731**	$ **25,610**
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of deferred loan origination fees, net of costs	486	297
Amortization of fair value discounts on acquired loans	3,504	-
Amortization of investment securities premiums, net of accretion of discounts	12,624	25,558
Amortization of core deposit and customer relationship intangibles	1,288	75
Amortization of fair value premiums on acquired deposits	9,649	-
FDIC shared-loss expense, net	32,836	10,410
Amortization of prepaid FDIC assessment	-	2,613
Other impairments on securities	7	-
Depreciation and amortization of premises and equipment	5,265	2,373
Deferred income taxes, net	(30,776)	(420)
Provision for covered and non-covered loan and lease losses, net	47,326	15,424
Stock-based compensation	888	787
(Gain) loss on:		
Sale of securities	-	(19,338)
Sale of mortgage loans held for sale	(1,771)	(2,898)
Derivatives	(1,271)	108
Early extinguishment of subordinated capital notes	(1,061)	-
Foreclosed real estate	3,109	1,284
Sale of other repossessed assets	464	-
Sale of premises and equipment	-	(86)
Originations of loans held-for-sale	(179,127)	(93,940)
Proceeds from sale of loans held-for-sale	68,809	49,388
Net (increase) decrease in:		
Trading securities	(1,714)	(34)
Accrued interest receivable	46	2,924
Servicing assets	(2,199)	(322)
Other assets	20,730	4,259
Net increase (decrease) in:		
Accrued interest on deposits and borrowings	(995)	(4,498)
Accrued expenses and other liabilities	12,093	(13,167)
Net cash provided by operating activities	**58,941**	**6,407**
Cash flows from investing activities:		
Purchases of:		

Investment securities available-for-sale	(17,802)	(558,201)
Investment securities held-to-maturity	-	(119,025)
FHLB stock	(12,465)	-
Maturities and redemptions of:		
Investment securities available-for-sale	313,866	378,144
Investment securities held-to-maturity	-	102,251
FHLB stock	28,720	911
Proceeds from sales of:		
Investment securities available-for-sale	75,660	553,602
Foreclosed real estate	18,219	4,639
Other repossessed assets	12,912	1,941
Premises and equipment	1,667	368
Origination and purchase of loans, excluding loans held-for-sale	(422,590)	(112,974)
Principal repayment of loans, including covered loans	528,274	128,340
Reimbursements from the FDIC on shared-loss agreements	18,696	39,729
Additions to premises and equipment	(6,237)	(1,225)
Net change in securities purchased under agreements to resell	80,000	(225,000)
Net cash provided by investing activities	**618,920**	**193,500**

OFG BANCORP

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS – (Continued)

FOR THE SIX-MONTH PERIODS ENDED JUNE 30, 2013 AND 2012

	Six-Month Period Ended June 30,			
	2013		2012	
	(In thousands)			
Cash flows from financing activities:				
Net increase (decrease) in:				
Deposits		(36,125)		(212,846)
Short term borrowings		(92,210)		-
Securities sold under agreements to repurchase		(381,358)		-
FHLB advances		(231,617)		5,070
Subordinated capital notes		(46,017)		-
FDIC-guaranteed term notes		-		(105,000)
Exercise of stock options		185		394
Issuance of common stock costs		(16)		-
Issuance of preferred stock costs		(23)		-
Purchase of treasury stock		-		(7,022)
Termination of derivative instruments		1,348		(124)
Dividends paid on preferred stock		(6,931)		(2,401)
Dividends paid on common stock		(5,479)		(4,886)
Net cash used in financing activities		**(798,243)**		**(326,815)**
Net change in cash and cash equivalents		**(120,382)**		**(126,908)**
Cash and cash equivalents at beginning of period		868,695		591,487
Cash and cash equivalents at end of period	**$**	**748,313**	**$**	**464,579**
Supplemental Cash Flow Disclosure and Schedule of Non-cash Activities:				
Interest paid	$	40,491	$	63,266
Income taxes paid	$	378	$	8,031
Mortgage loans securitized into mortgage-backed securities	$	89,590	$	37,730
Transfer from loans to foreclosed real estate and other repossessed assets	$	45,714	$	11,723
Securities sold but not yet delivered	$	16,732	$	-
Reclassification of loans held for investment portfolio to held for sale portfolio	$	40,328	$	5,182

See notes to unaudited consolidated financial statements

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – ORGANIZATION, CONSOLIDATION AND BASIS OF PRESENTATION

Nature of Operations

OFG Bancorp (the "Company") is a publicly-owned financial holding company incorporated under the laws of the Commonwealth of Puerto Rico. The Company operates through various subsidiaries including, a commercial bank, Oriental Bank (or the "Bank"), two broker-dealers, Oriental Financial Services Corp. ("Oriental Financial Services") and OFS Securities, Inc. ("OFS Securities"), an insurance agency, Oriental Insurance, Inc. ("Oriental Insurance") and a retirement plan administrator, Caribbean Pension Consultants, Inc. ("CPC"). The Company also has a special purpose entity, Oriental Financial (PR) Statutory Trust II (the "Statutory Trust II"). Through these subsidiaries and their respective divisions, the Company provides a wide range of banking and financial services such as commercial, consumer and mortgage lending, leasing, auto loans, financial planning, insurance sales, money management and investment banking and brokerage services, as well as corporate and individual trust services. On April 25, 2013, the Company changed its corporate name from Oriental Financial Group Inc. to OFG Bancorp.

On December 18, 2012, the Company purchased from Banco Bilbao Vizcaya Argentaria, S. A. ("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"), an insurance agency, and (ii) BBVA Securities of Puerto Rico, Inc. ("BBVA Securities," now known as "OFS 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."

Basis of Presentation and Use of Estimates

The accounting and reporting policies of the Company conform with U.S. generally accepted accounting principles ("GAAP") and to banking industry practices.

The unaudited consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") for interim financial information and should be read in conjunction with the audited consolidated financial statements in our annual report on Form 10-K for the year ended December 31, 2012 ("2012 Form 10-K"). All significant intercompany balances and transactions have been eliminated in consolidation. These unaudited statements are, in the opinion of management, a fair statement of the results for the periods reported and include all necessary adjustments, all of a normal recurring nature, for a fair statement of such results. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to SEC rules and regulations. Management believes that the disclosures made are adequate to make the information presented not misleading. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the unaudited consolidated financial statements and related disclosures. These estimates are based on information available as of the date of the consolidated financial statements. While management makes its best judgment, actual amounts or results could differ from these estimates. Interim period results are not necessarily indicative of the results to be expected for the full year.

Certain reclassifications have been made to 2012 unaudited consolidated financial statements and notes to the financial statements to conform to the 2013 presentation.

Significant Accounting Policies

We provide a summary of our significant accounting policies in our 2012 Form 10-K under "Notes to Consolidated Financial Statements—Note 1—Summary of Significant Accounting Policies." Below we describe recent accounting changes.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income - In February 2013, the FASB issued an amendment to enhance current disclosure requirements of reclassifications out of accumulated other comprehensive income and their corresponding effect on net income to be presented, in one place, information about significant amounts reclassified and, in some cases, cross-reference to related footnote disclosures. Previously, this information was presented in different places throughout the financial statements. The amendments require disclosure of information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, they require the presentation, either on the face of the statement where net income is presented or in the notes, of significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under GAAP to be reclassified in their entirety to net income, the Company is required to cross-reference to other disclosures required under GAAP that provide additional detail about those amounts. The amended guidance was effective for annual and interim reporting periods beginning on or after December 15, 2012, prospectively. Our adoption of the guidance is presented in "Note 13 – Stockholders' Equity and Earnings per Share."

Testing Indefinite-Lived Intangible Assets for Impairment - In July 2012, the FASB issued ASU No. 2012-02, *Intangibles—*

Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment. The ASU is intended to simplify the guidance for testing the decline in the realizable value (impairment) of indefinite-lived intangible assets other than goodwill. Some examples of intangible assets subject to the guidance include indefinite-lived trademarks, licenses and distribution rights. The ASU allows companies to perform a qualitative assessment about the likelihood of impairment of an indefinite-lived intangible asset to determine whether further impairment testing is necessary, similar in approach to the goodwill impairment test. The ASU became effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Our adoption of the guidance had no effect on our unaudited consolidated financial statements.

Offsetting Financial Assets and Liabilities - In December 2011, the FASB issued ASU No. 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities*. The ASU is intended to enhance current disclosure requirements on offsetting financial assets and liabilities. The new disclosures enable financial statement users to compare balance sheets prepared under GAAP and IFRS, which are subject to different offsetting models. The guidance requires disclosure of both gross and net information about instruments and transactions eligible for offset in the balance sheet as well as instruments and transactions subject to an agreement similar to a master netting arrangement. The disclosures are required irrespective of whether such instruments are presented gross or net on the balance sheet. In January 2013, the FASB issued ASU No. 2013-01, *Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*, which clarify that the scope of this guidance applies to derivatives accounted for in accordance with Topic 815, Derivatives and Hedging, including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with Section 210-20-45 or Section 815-10-45 or subject to an enforceable master netting arrangement or similar agreement. The amended guidance was effective for annual and interim reporting periods beginning on or after January 1, 2013, with comparative retrospective disclosures required for all periods presented. We adopted the guidance in the first quarter of 2013. Our adoption of the guidance had no effect on our financial condition, results of operations or liquidity since it only impacts disclosures only. The new disclosures required by the amended guidance are included in “Note 17 – Offsetting Arrangements” hereto.

Subsequent Accounting for an Indemnification Asset Recognized at the Acquisition Date as a Result of a Government-Assisted Acquisition of a Financial Institution— FASB ASU 2012-06, “Business Combinations” (Topic 805) was issued in October 2012. This update addresses the diversity in practice about how to interpret the terms “on the same basis” and “contractual limitations” when subsequently measuring an indemnification asset recognized in a government-assisted (Federal Deposit Insurance Corporation) acquisition of a financial institution that includes a loss-sharing agreement (indemnification agreement). When a reporting entity recognizes an indemnification asset as a result of a government-assisted acquisition of a financial institution and subsequently the cash flows expected to be collected on the indemnification asset change as a result of a change in cash flows expected to be collected on the assets subject to indemnification, the reporting entity should subsequently account for the change in the measurement of the indemnification asset on the same basis as the change in the assets subject to indemnification. Any amortization of changes in value should be limited to the contractual term of the indemnification agreement, that is, the lesser of the term of the indemnification agreement and the remaining life of the indemnified assets. The amendments in this update are effective for fiscal years and interim periods within those years, beginning on or after December 15, 2012. The adoption of this guidance did not have a material effect on the unaudited consolidated financial statements, since the Company already followed the same basis approach.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Future Application of Accounting Standards

Accounting for Financial Instruments—Credit Losses - In December 2012, the FASB issued a proposed ASU, *Financial Instruments—Credit Losses.* This proposed ASU, or exposure draft, was issued for public comment in order to allow stakeholders the opportunity to review the proposal and provide comments to the FASB, and does not constitute accounting guidance until a final ASU is issued. The exposure draft contains proposed guidance developed by the FASB with the goal of improving financial reporting about expected credit losses on loans, securities and other financial assets held by banks, financial institutions, and other public and private organizations. The exposure draft proposes a new accounting model intended to require earlier recognition of credit losses, while also providing additional transparency about credit risk. The FASB's proposed model would utilize a single "expected credit loss" measurement objective for the recognition of credit losses, replacing the multiple existing impairment models in GAAP which generally require that a loss be "incurred" before it is recognized. The FASB's proposed model represents a significant departure from existing GAAP, and may result in material changes to the Company's accounting for financial instruments. The impact of the FASB's final ASU to the Company's financial statements will be assessed when it is issued. The exposure draft does not contain a proposed effective date. This would be included in the final ASU, when issued.

Other Potential Amendments to Current Accounting Standards - The FASB and International Accounting Standards Board, either jointly or separately, are currently working on several major projects, including amendments to existing accounting standards governing financial instruments, leases, and consolidation and investment companies. As part of the joint financial instruments project, the FASB has issued a proposed ASU that would result in significant changes to the guidance for recognition and measurement of financial instruments, in addition to the proposed ASU that would change the accounting for credit losses on financial instruments discussed above. The FASB is also working on a joint project that would require substantially all leases to be capitalized on the balance sheet. Additionally, the FASB has issued a proposal on principal-agent considerations that would change the way the Company needs to evaluate whether to consolidate Variable Interest Entities ("VIE") and non-VIE partnerships. Furthermore, the FASB has issued a proposed ASU that would change the criteria used to determine whether an entity is subject to the accounting and reporting requirements of an investment company. The principal-agent consolidation proposal would require all VIEs, including those that are investment companies, to be evaluated for consolidation under the same requirements. All of these projects may have significant impacts for the Company. Upon completion of the standards, the Company will need to reevaluate its accounting and disclosures. However, due to ongoing deliberations of the standard setters, the Company is currently unable to determine the effect of future amendments or proposals.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 2 – BUSINESS COMBINATIONS

BBVAPR Acquisition

On December 18, 2012, the Company purchased from BBVA, all of the outstanding common stock of each of BBVAPR Holding and BBVA Securities for an aggregate purchase price of $500 million. Immediately following the closing of the BBVAPR Acquisition, the Company merged BBVAPR Bank with and into Oriental Bank, with Oriental Bank continuing as the surviving entity.

The assets acquired and liabilities assumed as of December 18, 2012 were presented at their fair value. In many cases, the determination of these fair values required management to make estimates about discount rates, expected cash flows, market conditions and other future events that are highly subjective in nature and subject to change. The fair values initially assigned to the assets acquired and liabilities assumed were preliminary and subject to refinement for up to one year after the closing date of the acquisition as new information relative to closing date fair values became available. During the quarter ended June 30, 2013, the Company recorded retrospective adjustments to the preliminary estimated fair values of certain acquired loans, foreclosed real estate, deferred income taxes, and other assets acquired, to reflect new information obtained during the measurement period (as defined by ASC Topic 805), about facts and circumstances that existed as of the acquisition date that, if known, would have affected the acquisition-date fair value measurements. As detailed in the table below, the main adjustment occurred in the loans acquired. The adjustment resulted from in-depth reviews of the actual terms and amortization schedules. The original cash flows were revised to reflect the results of this review.

Net-assets acquired and their respective measurement period adjustments are reflected in the table below:

	Book Value December 18, 2012	Fair Value Adjustments, net	Fair Value December 18, 2012	Measurement Period Adjustments, net June 30, 2013	Fair Value as Remeasured June 30, 2013
			(In thousands)		
Assets					
Cash and cash equivalents	$ 394,638	$ -	$ 394,638	$ -	$ 394,638
Investments	561,623	-	561,623	-	561,623
Loans	3,678,979	(118,913)	3,560,066	(12,798)	3,547,268
Accrued interest receivable	19,133	(18,252)	881	-	881
Foreclosed real estate	44,853	(8,896)	35,957	(1,932)	34,025
Deferred tax asset, net	35,327	50,005	85,332	5,300	90,632
Premises and equipment	37,412	29,067	66,479	-	66,479
Legacy goodwill	116,353	(116,353)	-	-	-

Core deposit intangible		-		8,473		8,473		-		8,473
Customer relationship intangible		-		5,060		5,060		-		5,060
Other assets		119,286		(7,663)		111,623		(2,936)		108,687
Total assets acquired		**5,007,604**		**(177,472)**		**4,830,132**		**(12,366)**		**4,817,766**
Liabilities										
Deposits		3,472,951		21,489		3,494,440		-		3,494,440
Securities sold under agreements to repurchase		338,020		20,465		358,485		-		358,485
Other borrowings		348,624		1,108		349,732		-		349,732
Subordinated capital notes		117,000		(7,159)		109,841		-		109,841
Accrued expenses and other liabilities		80,392		(1,438)		78,954		-		78,954
Total liabilities assumed		**4,356,987**		**34,465**		**4,391,452**		**-**		**4,391,452**
Net assets acquired	**$**	**650,617**	**$**	**(211,937)**	**$**	**438,680**	**$**	**(12,366)**	**$**	**426,314**
Cash consideration	**$**	**500,000**	**$**	**-**	**$**	**500,000**	**$**	**-**	**$**	**500,000**
Goodwill					**$**	**61,320**	**$**	**12,366**	**$**	**73,686**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Merger and Restructuring Charges

Merger and restructuring charges are recorded in the unaudited consolidated statement of operations and include incremental costs to integrate the operations of the Company and BBVAPR. These charges represent costs associated with these one-time activities and do not represent ongoing costs of the fully integrated combined organization.

The following table presents severance and employee-related charges, systems integrations and other merger-related charges in connection with the BBVAPR Acquisition for the quarter and six-month period ended June 30, 2013:

	Quarter Ended June 30, 2013 (In thousands)		Six-Month Period Ended June 30, 2013 (In thousands)	
Severance and employee-related charges	$	400	$	1,150
Systems integrations and related charges		2,231		3,177
Other-contract cancellation fee		2,643		6,481
Total merger and restructuring charges	**$**	**5,274**	**$**	**10,808**

Restructuring Reserve

Restructuring reserves are established by a charge to merger and restructuring charges, and the restructuring charges are included in the merger and restructuring charges table.

The following table presents the changes in restructuring reserves for the quarter and six-month period ended June 30, 2013:

	Quarter Ended June 30, 2013 (In thousands)		Six-Month Period Ended June 30, 2013 (In thousands)	
Balance at the beginning of the period	$	6,336	$	4,202
Merger and restructuring charges		5,274		10,808
Cash payments and other		(11,334)		(14,734)
Balance at the end of the period	**$**	**276**	**$**	**276**

Payments under merger and restructuring reserves associated with the BBVAPR Acquisition are expected to continue in 2013 and will be accounted under applicable accounting guidance to the cost being incurred.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The FDIC-Assisted Acquisition and FDIC Shared-Loss Indemnification Asset

On April 30, 2010, the Bank acquired certain assets and assumed certain deposits and other liabilities in the FDIC-assisted acquisition of Eurobank. These assets acquired and liabilities assumed were recorded at fair value on the date of acquisition. As part of the Purchase and Assumption Agreement between the Bank and the FDIC (the "Purchase and Assumption Agreement"), the Bank and the FDIC entered into shared-loss agreements, whereby the FDIC covers a substantial portion of any losses on loans (and related unfunded loan commitments), foreclosed real estate and other repossessed properties.

The acquired loans, foreclosed real estate, and other repossessed property subject to the shared-loss agreements are collectively referred to as "covered assets." Under the terms of the shared-loss agreements, the FDIC absorbs 80% of losses and shares in 80% of loss recoveries on covered assets. The term of the shared-loss agreement covering single family residential mortgage loans is ten years with respect to losses and loss recoveries, while the term of the shared-loss agreement covering commercial loans is five years with respect to losses and eight years with respect to loss recoveries, from the April 30, 2010 acquisition date. The shared-loss agreements also provide for certain costs directly related to the collection and preservation of covered assets to be reimbursed at an 80% level. The indemnification asset represents the portion of estimated losses covered by the shared-loss agreements between the Bank and the FDIC.

The Bank agreed to make a true-up payment, also known as clawback liability, to the FDIC on the date that is 45 days following the last day (such day, the "True-Up Measurement Date") of the final shared-loss month, or upon the final disposition of all covered assets under the shared-loss agreements in the event losses thereunder fail to reach expected levels. Under the shared-loss agreements, the Bank will pay to the FDIC 50% of the excess, if any, of: (i) 20% of the Intrinsic Loss Estimate of $906.0 million (or $181.2 million) (as determined by the FDIC) less (ii) the sum of: (A) 25% of the asset discount (per bid) (or $227.5 million); plus (B) 25% of the cumulative shared-loss payments (defined as the aggregate of all of the payments made or payable to the Bank minus the aggregate of all of the payments made or payable to the FDIC); plus (C) the sum of the period servicing amounts for every consecutive twelve-month period prior to and ending on the True-Up Measurement Date in respect of each of the shared-loss agreements during which the shared-loss provisions of the applicable shared-loss agreement is in effect (defined as the product of the simple average of the principal amount of shared-loss loans and shared-loss assets at the beginning and end of such period times 1%). The true-up payment represents an estimated liability of $16.9 million and $15.5 million, net of discount, as of June 30, 2013 and December 31, 2012, respectively. This estimated liability is accounted for as a reduction of the indemnification asset.

The FDIC shared-loss indemnification asset activity for the six-month periods ended June 30, 2013 and 2012 follows:

	Six-Month Period Ended June 30,	
	2013	2012
	(In thousands)	
Balance at beginning of period	$ 286,799	$ 392,367
Shared-loss agreements reimbursements from the FDIC	(18,696)	(39,729)
Increase (decrease) in expected credit losses to be covered under shared-loss agreements, net	(2,015)	12,748
FDIC shared-loss expense, net	(32,836)	(10,410)
Incurred expenses to be reimbursed under shared-loss agreements	3,220	4,791
Balance at end of period	**$ 236,472**	**$ 359,767**

During the quarter ended June 30, 2013, the Company recorded $7.1 million in additional amortization of the FDIC indemnification asset from stepped up costs recoveries on certain construction and leasing pools.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 3 – SECURITIES PURCHASED UNDER AGREEMENTS TO RESELL AND INVESTMENTS

Money Market Investments

The Company considers as cash equivalents all money market instruments that are not pledged and that have maturities of three months or less at the date of acquisition. At June 30, 2013 and December 31, 2012, money market instruments included as part of cash and cash equivalents amounted to $11.0 million and $13.2 million, respectively.

Securities Purchased Under Agreements to Resell

Securities purchased under agreements to resell consist of short-term investments and are carried at the amounts at which the assets will be subsequently resold as specified in the respective agreements. At December 31, 2012, securities purchased under agreements to resell amounted to $80.0 million. The fair value of the collateral securities held by the Company on these transactions as of December 31, 2012 was approximately $82.1 million. On June 30, 2013 the Company had no securities purchased under agreements to resell.

Investment Securities

The amortized cost, gross unrealized gains and losses, fair value, and weighted average yield of the securities owned by the Company at June 30, 2013 and December 31, 2012 were as follows:

	June 30, 2013				
	Amortized Cost	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**	**Weighted Average Yield**
			(In thousands)		
Available-for-sale					
Mortgage-backed securities					
FNMA and FHLMC certificates	$ 1,358,834	$ 36,112	$ 4,324	$ 1,390,622	2.92%
GNMA certificates	10,590	604	13	11,180	4.88%
CMOs issued by US Government sponsored agencies	250,806	85	2,528	248,363	1.81%
	1,620,230	**36,801**	**6,865**	**1,650,165**	**2.76%**

Total mortgage-backed securities								
Investment securities								
US Treasury securities	26,499		2		-		26,501	0.08%
Obligations of US Government sponsored agencies	15,078		35		-		15,113	1.23%
Obligations of Puerto Rico Government and political subdivisions	120,989		-		1,294		119,695	4.42%
Other debt securities	24,539		216		-		24,755	3.45%
Total investment securities	**187,105**		**253**		**1,294**		**186,064**	**3.42%**
Total securities available for sale	**$ 1,807,335**	**$**	**37,054**	**$**	**8,159**	**$**	**1,836,229**	**2.83%**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2012				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Weighted Average Yield
	(In thousands)				
Available-for-sale					
Mortgage-backed securities					
FNMA and FHLMC certificates	$ 1,622,037	$ 71,411	$ 1	$ 1,693,447	3.06%
GNMA certificates	14,177	995	8	15,164	4.89%
CMOs issued by US Government sponsored agencies	288,409	3,784	793	291,400	1.85%
Total mortgage-backed securities	**1,924,623**	**76,190**	**802**	**2,000,011**	**2.89%**
Investment securities					
US treasury securities	26,498	-	2	26,496	0.71%
Obligations of US Government sponsored agencies	21,623	224	-	21,847	1.35%
Obligations of Puerto Rico Government and political subdivisions	120,950	9	438	120,521	3.82%
Other debt securities	25,131	280	-	25,411	3.46%
Total investment securities	**194,202**	**513**	**440**	**194,275**	2.99%
Total securities available-for-sale	**$ 2,118,825**	**$ 76,703**	**$ 1,242**	**$ 2,194,286**	**2.90%**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The amortized cost and fair value of the Company's investment securities at June 30, 2013, by contractual maturity, are shown in the next table. Securities not due on a single contractual maturity date, such as collateralized mortgage obligations, are classified in the period of final contractual maturity. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	June 30, 2013 Available-for-sale	
	Amortized Cost	Fair Value
	(In thousands)	
Mortgage-backed securities		
Due after 5 to 10 years		
FNMA and FHLMC certificates	$ 32,779	$ 33,345
Total due after 5 to 10 years	**32,779**	**33,345**
Due after 10 years		
FNMA and FHLMC certificates	1,326,055	1,357,277
GNMA certificates	10,590	11,180
CMOs issued by US Government sponsored agencies	250,806	248,363
Total due after 10 years	**1,587,451**	**1,616,820**
Total mortgage-backed securities	**1,620,230**	**1,650,165**
Investment securities		
Due in less than one year		
US Treasury securities	26,499	26,501
Other debt securities	20,000	20,058
Total due in less than one year	**46,499**	**46,559**
Due from 1 to 5 years		
Obligations of Puerto Rico Government and political subdivisions	412	399
Total due from 1 to 5 years	**412**	**399**
Due after 5 to 10 years		
Obligations of Puerto Rico Government and political subdivisions	11,425	11,053
Obligations of US Government and sponsored agencies	15,078	15,113
Total due after 5 to 10 years	**26,503**	**26,166**
Due after 10 years		
Obligations of Puerto Rico Government and political subdivisions	109,152	108,243
Other debt securities	4,539	4,697
Total due after 10 years	**113,691**	**112,940**
Total investment securities	**187,105**	**186,064**
Total securities available-for-sale	**$ 1,807,335**	**$ 1,836,229**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The BBVAPR Acquisition and the related deleverage of the investment securities portfolio that the Company completed during the second half of 2012 reduced the interest rate risk profile of the Company. During the six-month period ended June 30, 2013, the Company did not execute any sale of securities from its portfolio other than $92.4 million of available-for-sale GNMA certificates that were sold as part of its recurring mortgage loan origination and securitization activities. These sales produced a nominal gain during such period. During the six-month period ended June 30, 2012, there were certain sales of available-for-sale securities because the Company believed that gains could be realized and that there were good opportunities to invest the proceeds in other investment securities with attractive yields and terms that would allow the Company to continue protecting its net interest margin.

The Company, as part of its asset/liability management, may purchase U.S. Treasury securities and U.S. government sponsored agency discount notes close to their maturities as alternatives to cash deposits at correspondent banks or as a short term vehicle to reinvest the proceeds of sale transactions until investment securities with attractive yields can be purchased.

For the six-month period ended June 30, 2012, the Company recorded a net gain on sale of securities of $19.3 million. The table below presents the gross realized gains by category for such period:

	Six-Month period Ended June 30, 2012			
Description	**Sale Price**	**Book Value at Sale**	**Gross Gains**	**Gross Losses**
		(In thousands)		
Sale of securities available-for-sale				
Mortgage-backed securities and CMOs				
FNMA and FHLMC certificates	$ 367,971	$ 349,400	$ 18,581	$ -
GNMA certificates	39,484	39,483	1	-
CMOs issued by US Government sponsored agencies	19,725	18,372	1,353	-
Total mortgage-backed securities and CMOs	427,180	407,255	19,935	-
Investment securities				
Obligations of U.S. Government sponsored agencies	80,000	80,000	-	-
Obligations of Puerto Rico Government and political subdivisions	35,882	36,478	31	628
Structured credit investments	10,530	10,530	-	-
Total investment securities	126,412	127,008	31	628
Total	**$ 553,592**	**$ 534,263**	**$ 19,966**	**$ 628**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following tables show the Company's gross unrealized losses and fair value of investment securities available-for-sale, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2013 and December 31, 2012:

	June 30, 2013		
	12 months or more		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
Obligations of Puerto Rico Government and political subdivisions	$ 1,712	61	1,651
CMOs issued by US Government sponsored agencies	2,094	171	1,923
	$ **3,806**	$ **232**	$ **3,574**

	Less than 12 months		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
Obligations of Puerto Rico Government and political subdivisions	$ 20,588	$ 1,233	$ 19,355
CMOs issued by US Government sponsored agencies	203,524	2,357	201,167
FNMA and FHLMC certificates	219,983	4,324	215,659
GNMA certificates	206	13	193
	$ 444,301	**$ 7,927**	**$ 436,374**

	Total		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
Obligations of Puerto Rico Government and political subdivisions	$ 22,300	$ 1,294	$ 21,006
CMOs issued by US Government sponsored agencies	205,618	2,528	203,090
FNMA and FHLMC certificates	219,983	4,324	215,659
GNMA certificates	206	13	193
	$ 448,107	**$ 8,159**	**$ 439,948**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2012 12 months or more		
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
Obligations of Puerto Rico Government and political subdivisions	$ 1,673	$ 12	$ 1,661
CMOs issued by US Government sponsored agencies	2,194	178	2,016
	$ 3,867	**$ 190**	**$ 3,677**

		Less than 12 months	
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
Obligations of Puerto Rico Government and political subdivisions	$ 19,086	$ 426	$ 18,660
CMOs issued by US Government sponsored agencies	10,671	615	10,056
US Treasury Securities	11,498	2	11,496
GNMA certificates	84	8	76
FNMA and FHLMC certificates	68	1	67
	$ 41,407	**$ 1,052**	**$ 40,355**

		Total	
	Amortized Cost	Unrealized Loss	Fair Value
		(In thousands)	
Securities available-for-sale			
Obligations of Puerto Rico Government and political subdivisions	$ 20,759	$ 438	$ 20,321
CMOs issued by US Government sponsored agencies	12,865	793	12,072
US Treasury Securities	11,498	2	11,496
GNMA certificates	84	8	76
FNMA and FHLMC certificates	68	1	67
	$ 45,274	**$ 1,242**	**$ 44,032**

The Company conducts quarterly reviews to identify and evaluate each investment in an unrealized loss position for other-than-temporary impairment. Any portion of a decline in value associated with credit loss is recognized in income with the remaining noncredit-related component recognized in other comprehensive income. A credit loss is determined by assessing whether the amortized cost basis of the security will be recovered by comparing the present value of cash flows expected to be collected from the security, discounted at the rate equal to the yield used to accrete current and prospective beneficial interest for the security. The shortfall of the present value of the cash flows expected to be collected in relation to the amortized cost basis is considered to be the “credit loss.” Other-than-temporary impairment analysis is based on estimates that depend on market conditions and are subject to further change over time. In addition, while the Company believes that the methodology used to value these exposures is reasonable, the methodology is subject to continuing refinement, including those made as a result of market developments. Consequently, it is reasonably possible that changes in estimates or conditions could result in the need to recognize additional other-than-temporary impairment charges in the future.

Securities in an unrealized loss position at June 30, 2013 are mainly composed of highly liquid securities that in most cases have a large and efficient secondary market. Valuations are performed on a monthly basis. The Company’s management believes that the unrealized losses of such securities at June 30, 2013 are temporary and are substantially related to market interest rate fluctuations and not to deterioration in the creditworthiness of the issuer or guarantor. At June 30, 2013, the Company does not have the intent to sell these investments in an unrealized loss position.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 4 - LOANS

The Company's loan portfolio is composed of covered loans and non-covered loans. The Company presents loans subject to the loss sharing agreements as "covered loans" in the information below, and loans that are not subject to FDIC loss sharing agreements as "non-covered loans." The risks of the Eurobank FDIC-assisted acquisition acquired loans are significantly different from those loans not covered under the FDIC loss sharing agreements because of the loss protection provided by the FDIC. Also, loans acquired in the BBVAPR Acquisition are included as non-covered loans in the unaudited consolidated statements of financial condition. Non-covered loans are further segregated between originated loans, acquired loans accounted for under ASC 310-20 (loans with revolving feature and/or acquired at a premium) and acquired loans accounted for under ASC 310-30 (loans acquired with deteriorated credit quality, including those by analogy).

For a summary of the accounting policy related to loans, interest recognition and allowance for loan and lease losses, please refer to the summary of significant accounting policies included in Note 1 of our 2012 Form 10-K under "Notes to Consolidated Financial Statements".

The composition of the Company's loan portfolio at June 30, 2013 and December 31, 2012 was as follows:

	June 30, 2013	December 31, 2012
	(In thousands)	
Loans not covered under shared-loss agreements with FDIC:		
Originated and other loans and leases held for investment:		
Mortgage	$ 755,298	$ 804,942
Commercial	702,074	353,930
Auto and leasing	233,092	50,720
Consumer	89,608	48,136
	1,780,072	**1,257,728**
Acquired loans:		
Accounted for under ASC 310-20 (Loans with revolving feature and/or acquired at a premium)		
Commercial	140,234	317,244
Commercial secured by real estate	14,519	29,215
Auto	373,587	457,894
Consumer	62,751	68,878
	591,091	**873,231**

Accounted for under ASC 310-30 (Loans acquired with deteriorated credit quality, including those by analogy)				
Commercial		747,077		942,267
Construction		140,060		196,692
Mortgage		781,389		810,135
Auto		462,691		554,938
Consumer		88,375		118,171
		2,219,592		**2,622,203**
		4,590,755		**4,753,162**
Deferred loan fees, net		(831)		(3,463)
Loans receivable		**4,589,924**		**4,749,699**
Allowance for loan and lease losses on non-covered loans		(46,625)		(39,921)
Loans receivable, net		**4,543,299**		**4,709,778**
Mortgage loans held-for-sale		78,350		64,145
Total loans not covered under shared-loss agreements with FDIC, net		**4,621,649**		**4,773,923**
Loans covered under shared-loss agreements with FDIC:				
Loans secured by 1-4 family residential properties		123,507		128,811
Construction and development secured by 1-4 family residential properties		16,478		15,969
Commercial and other construction		275,489		289,070
Leasing		943		7,088
Consumer		6,955		8,493
Total loans covered under shared-loss agreements with FDIC		**423,372**		**449,431**
Allowance for loan and lease losses on covered loans		(53,992)		(54,124)
Total loans covered under shared-loss agreements with FDIC, net		**369,380**		**395,307**
Total loans, net	**$**	**4,991,029**	**$**	**5,169,230**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Non-covered Loans

Originated and Other Loans and Leases Held for Investment

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

The following table presents the aging of the recorded investment in gross originated and other loans held for investment as of June 30, 2013 and December 31, 2012 by class of loans. Mortgage loans past due included delinquent loans in the GNMA buy-back option program. Servicers of loans underlying GNMA mortgage-backed securities must report as their own assets the defaulted loans that they have the option (but not the obligation) to repurchase, even when they elect not to exercise that option.

	June 30, 2013						
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	Loans 90+ Days Past Due and Still Accruing
	(In thousands)						
Mortgage							
Traditional (by origination year):							
Up to the year 2002	$ -	$ 2,937	$ 6,993	$ 9,930	$ 79,666	$ 89,596	$ 6
Years 2003 and 2004	-	5,413	3,429	8,842	117,754	126,596	-
Year 2005	-	2,136	1,431	3,567	65,196	68,763	-
Year 2006	-	3,369	2,838	6,207	87,614	93,821	-
Years 2007, 2008 and 2009	-	2,863	3,407	6,270	104,169	110,439	433

Years 2010, 2011, 2012	-	391	2,115	2,506	96,270	98,776	76
and 2013	-	17,109	20,213	37,322	550,669	587,991	515
Non-traditional	-	1,520	2,212	3,732	42,695	46,427	-
Loss mitigation program	-	4,993	14,287	19,280	68,335	87,615	1,606
	-	23,622	36,712	60,334	661,699	722,033	2,121
Home equity secured personal loans	-	-	12	12	740	752	-
GNMA's buy-back option program	-	-	32,513	32,513	-	32,513	-
	-	**23,622**	**69,237**	**92,859**	**662,439**	**755,298**	**2,121**
Commercial							
Commercial secured by real estate	11,033	1,381	12,694	25,108	386,236	411,344	-
Other commercial and industrial	324	66	753	1,143	289,587	290,730	-
	11,357	**1,447**	**13,447**	**26,251**	**675,823**	**702,074**	**-**
Consumer	**670**	**165**	**370**	**1,205**	**88,403**	**89,608**	**-**
Auto and leasing	**8,826**	**2,075**	**1,096**	**11,997**	**221,095**	**233,092**	**-**
Total	**$ 20,853**	**$ 27,309**	**$ 84,150**	**$ 132,312**	**$ 1,647,760**	**$ 1,780,072**	**$ 2,121**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	December 31, 2012						
	30-59 Days Past Due	**60-89 Days Past Due**	**90+ Days Past Due**	**Total Past Due**	**Current**	**Total Loans**	**Loans 90+ Days Past Due and Still Accruing**
				(In thousands)			
Mortgage							
Traditional (by origination year):							
Up to the year 2002	$ 6,906	$ 2,116	$ 11,363	$ 20,385	$ 80,883	$ 101,268	$ -
Years 2003 and 2004	12,048	5,206	18,162	35,416	114,446	149,862	-
Year 2005	4,983	1,746	8,860	15,589	65,312	80,901	-
Year 2006	9,153	3,525	15,363	28,041	85,045	113,086	-
Years 2007, 2008 and 2009	2,632	1,682	8,965	13,279	108,358	121,637	-
Years 2010, 2011 and 2012 and 2012	632	769	1,162	2,563	64,084	66,647	-
	36,354	15,044	63,875	115,273	518,128	633,401	-
Non-traditional	2,850	1,067	11,160	15,077	42,742	57,819	-
Loss mitigation program	8,933	4,649	19,989	33,571	53,739	87,310	
	48,137	20,760	95,024	163,921	614,609	778,530	-
Home equity secured personal loans	-	-	10	10	726	736	-
GNMA's buy-back option program	-	-	25,676	25,676	-	25,676	-
	48,137	**20,760**	**120,710**	**189,607**	**615,335**	**804,942**	**-**
Commercial							
	9,062	271	15,335	24,668	226,606	251,274	-

Commercial secured by real estate							
Other commercial and industrial	345	189	2,378	2,912	99,744	102,656	-
	9,407	**460**	**17,713**	**27,580**	**326,350**	**353,930**	**-**
Consumer	**747**	**92**	**409**	**1,248**	**46,888**	**48,136**	-
Auto and leasing	**251**	**129**	**131**	**511**	**50,209**	**50,720**	**-**
Total	**$ 58,542**	**$ 21,441**	**$ 138,963**	**$ 218,946**	**$ 1,038,782**	**$ 1,257,728**	**$ -**

During the quarter ended June 30, 2013, the Company transferred $55.0 million of non-performing residential mortgage loans held-for-investment to held-for-sale at a fair value of $27.0 million. The difference between fair value and book value was recorded as charge-off to the mortgage portfolio. The provision for loan and lease losses during the quarter and six-month period ended June 30, 2013 increased to provide the coverage necessary under the allowance policy for the remaining mortgage loans, following the effects that the aforementioned reclassification had on the mortgage portfolio allowance level.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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

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

The following table presents the aging of the recorded investment in gross acquired loans accounted for under ASC 310-20 as of June 30, 2013 and December 31, 2012 by class of loans:

	June 30, 2013						
	30-59 Days Past Due	**60-89 Days Past Due**	**90+ Days Past Due**	**Total Past Due**	**Current**	**Total Loans**	**Loans 90+ Days Past Due and Still Accruing**
	(In thousands)						
Commercial	$ 291	$ 134	$ 493	$ 918	$ 139,316	$ 140,234	$ -
Commercial secured by real estate	9	-	-	9	14,510	14,519	-
Auto	8,849	1,892	674	11,415	362,172	373,587	-
Consumer	1,767	7	1,069	2,843	59,908	62,751	-
Total	**$ 10,916**	**$ 2,033**	**$ 2,236**	**$ 15,185**	**$ 575,906**	**$ 591,091**	**$ -**

December 31, 2012

Loans 90+

	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	Days Past Due and Still Accruing
			(In thousands)				
Commercial	$ 715	$ 76	$ 193	$ 984	$ 316,260	$ 317,244	$ -
Commercial secured by real estate	315	-	-	315	28,900	29,215	-
Auto	6,753	1,023	275	8,051	449,843	457,894	-
Consumer	982	-	1,095	2,077	66,801	68,878	-
Total	**$ 8,765**	**$ 1,099**	**$ 1,563**	**$ 11,427**	**$ 861,804**	**$ 873,231**	**$ -**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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

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

The carrying amount corresponding to non-covered loans acquired with deteriorated credit quality, including those accounted under ASC 310-30 by analogy, in the statement of financial condition at June 30, 2013 and December 31, 2012 is as follows:

	June 30, 2013	December 31, 2012
	(In thousands)	
Contractual required payments receivable	$ 3,429,294	$ 3,954,484
Less: Non-accretable discount	713,641	741,872
Cash expected to be collected	2,715,653	3,212,612
Less: Accretable yield	496,061	590,409
Carrying amount	$ 2,219,592	$ 2,622,203

The following tables describe the accretable yield and non-accretable discount activity of acquired loans accounted for under ASC 310-30 for the quarter and six-month period ended June 30, 2013, excluding covered loans:

	Quarter Ended June 30, 2013		Six-Month Period Ended June 30, 2013	
	(In thousands)			
Accretable Yield Activity				
Balance at beginning of period	$	542,741	$	590,409
Accretion		(54,427)		(102,095)
Transfer from non-accretable discount		7,747		7,747
Balance at end of period	**$**	**496,061**	**$**	**496,061**

	Quarter Ended June 30, 2013	Six-Month Period Ended June 30, 2013
	(In thousands)	

Non-Accretable Discount Activity				
Balance at beginning of period	$	733,126	$	741,872
Principal losses		(11,738)		(20,484)
Transfer to accretable yield		(7,747)		(7,747)
Balance at end of period	**$**	**713,641**	**$**	**713,641**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Covered Loans

The carrying amount of covered loans at June 30, 2013 and December 31, 2012 is as follows:

		June 30, 2013		December 31, 2012
		(In thousands)		
Contractual required payments receivable	$	782,763	$	874,994
Less: Non-accretable discount		192,259		237,555
Cash expected to be collected		590,504		637,439
Less: Accretable yield		167,132		188,008
Carrying amount, gross		423,372		449,431
Less: Allowance for covered loan and lease losses		53,992		54,124
Carrying amount, net	**$**	**369,380**	**$**	**395,307**

The following tables describe the accretable yield and non-accretable discount activity of covered loans for the quarters and six-month periods ended June 30, 2013 and 2012:

	Quarter Ended June 30,				Six-Month Period Ended June 30,			
	2013		2012		2013		2012	
	(In thousands)				(In thousands)			
Accretable yield activity								
Balance at beginning of period	$	174,107	$	174,878	$	188,008	$	188,822
Accretion		(23,999)		(20,342)		(44,228)		(41,884)
Transfer from non-accretable discount		17,024		22,712		23,352		30,310
Balance at end of period	**$**	**167,132**	**$**	**177,248**	**$**	**167,132**	**$**	**177,248**

	Quarter Ended June 30,				Six-Month Period Ended June 30,			
	2013		2012		2013		2012	
	(In thousands)				(In thousands)			
Non-accretable discount activity								
Balance at beginning of period	$	214,236	$	379,780	$	237,555	$	412,170
Principal losses		(4,953)		(42,664)		(21,944)		(67,456)

Transfer to accretable yield	(17,024)	(22,712)	(23,352)	(30,310)
Balance at end of period	**$ 192,259**	**$ 314,404**	**$ 192,259**	**$ 314,404**

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Non-accrual Loans

The following table presents the recorded investment in loans in non-accrual status by class of loans as of June 30, 2013 and December 31, 2012:

	June 30, 2013		December 31, 2012	
	(In thousands)			
Originated and other loans and leases held for investment				
Mortgage				
Traditional (by origination year):				
Up to the year 2002	$	6,987	$	11,362
Years 2003 and 2004		3,465		18,162
Year 2005		1,481		8,859
Year 2006		2,875		15,363
Years 2007, 2008 and 2009		3,580		8,967
Years 2010, 2011, 2012 and 2013		3,988		1,162
		22,376		63,875
Non-traditional		2,287		11,160
Loss mitigation program		28,450		39,957
		53,113		114,992
Home equity secured personal loans		12		10
		53,125		**115,002**
Commercial				
Commercial secured by real estate		29,491		26,517
Other commercial and industrial		2,939		2,989
		32,430		**29,506**
Consumer		**370**		**442**
Auto and leasing		**1,096**		**131**
Acquired loans accounted under ASC 310-20				
Commercial		493		193
Auto		674		275
Consumer		1,069		1,095
		2,236		**1,563**
Total non-accrual loans	**$**	**89,257**	**$**	**146,644**

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

These loans do not include certain non-performing residential mortgage loans with a net book value of $55.0 million reclassified during the quarter ended June 30, 2013 to the loan held-for-sale category. Without this re-classification to loans held-for-sale, non-accruing loan balances would have been relatively consistent between December 31, 2012 and June 30, 2013.

Effective April 24, 2013, delinquent residential mortgage loans insured or guaranteed under applicable FHA and VA programs are placed in non-accrual when they become 18 months or more past due, since they are insured loans. Before that date, they were placed in non-accrual when they became 90 days or more past due.

At June 30, 2013 and December 31, 2012, loans whose terms have been extended and which are classified as troubled-debt restructurings that are not included in non-accrual loans amounted to $55.7 million and $52.0 million, respectively.

OFG BANCORP

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 5 - ALLOWANCE FOR LOAN AND LEASE LOSSES

Non-Covered Loans

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

Originated and Other Loans and Leases Held for Investment

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

	Quarter Ended June 30, 2013					
	Mortgage	**Commercial**	**Consumer**	**Auto and Leasing**	**Unallocated**	**Total**
	(In thousands)					
Allowance for loan and lease losses:						
Balance at beginning of period	$ 22,889	$ 16,314	$ 1,313	$ 1,741	$ 77	$ 42,334
Charge-offs	(29,120)	(2,886)	(323)	(709)	-	(33,038)
Recoveries	-	234	43	209	-	486
Provision for non-covered loan and lease losses	27,606	3,961	1,309	2,400	643	35,919
	$ 21,375	**$ 17,623**	**$ 2,342**	**$ 3,641**	**$ 720**	**$ 45,701**

Balance at end of period

	Six-Month Period Ended June 30, 2013					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	Total
	(In thousands)					
Allowance for loan and lease losses:						
Balance at beginning of period	$ 21,092	$ 17,072	$ 856	$ 533	$ 368	$ 39,921
Charge-offs	(31,707)	(3,444)	(569)	(800)	-	(36,520)
Recoveries	-	262	107	216	-	585
Provision for non-covered loan and lease losses	31,990	3,733	1,948	3,692	352	41,715
Balance at end of period	**$ 21,375**	**$ 17,623**	**$ 2,342**	**$ 3,641**	**$ 720**	**$ 45,701**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	June 30, 2013					
	Mortgage	Commercial	Consumer	Auto and Leasing	Unallocated	Total
	(In thousands)					
Allowance for loan and lease losses:						
Ending allowance balance attributable to loans:						
Individually evaluated for impairment	$ 8,879	$ 5,795	$ -	$ -	$ -	$ 14,674
Collectively evaluated for impairment	12,496	11,828	2,342	3,641	720	31,027
Total ending allowance balance	**$ 21,375**	**$ 17,623**	**$ 2,342**	**$ 3,641**	**$ 720**	**$ 45,701**
Loans:						
Individually evaluated for impairment	$ 81,849	$ 43,831	$ -	$ -	$ -	$ 125,680
Collectively evaluated for impairment	673,449	658,244	89,608	233,091	-	1,654,392
Total ending loan balance	**$ 755,298**	**$ 702,075**	**$ 89,608**	**$ 233,091**	**$ -**	**$ 1,780,072**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Quarter Ended June 30, 2012					
	Mortgage	**Commercial**	**Consumer**	**Leasing**	**Unallocated**	**Total**
	(In thousands)					
Allowance for loan and lease losses:						
Balance at beginning of period	$ 18,967	$ 15,045	$ 1,328	$ 510	$ 1,511	$ 37,361
Charge-offs	(1,948)	(1,721)	(184)	-	-	(3,853)
Recoveries	-	34	56	4	-	94
Provision for (recapture of) non-covered loan and lease losses	2,769	2,620	(202)	(317)	(1,070)	3,800
Balance at end of period	**$ 19,788**	**$ 15,978**	**$ 998**	**$ 197**	**$ 441**	**$ 37,402**

	Six-Month Period Ended June 30, 2012					
	Mortgage	**Commercial**	**Consumer**	**Leasing**	**Unallocated**	**Total**
	(In thousands)					
Allowance for loan and lease losses:						
Balance at beginning of period	$ 21,652	$ 12,548	$ 1,423	$ 845	$ 542	$ 37,010
Charge-offs	(2,869)	(3,358)	(366)	(31)	-	(6,624)
Recoveries	-	101	107	8	-	216
Provision for (recapture of) non-covered loan and lease losses	1,005	6,687	(166)	(625)	(101)	6,800
Balance at end of period	**$ 19,788**	**$ 15,978**	**$ 998**	**$ 197**	**$ 441**	**$ 37,402**

	December 31, 2012					
	Mortgage	**Commercial**	**Consumer**	**Auto and Leasing**	**Unallocated**	**Total**
	(In thousands)					
Allowance for loan and lease losses:						

Ending allowance balance attributable to loans:												
Individually evaluated for impairment	$	5,334	$	4,121	$	-	$	-	$	-	$	9,455
Collectively evaluated for impairment		15,758		12,951		856		533		368		30,466
Total ending allowance balance	**$**	**21,092**	**$**	**17,072**	**$**	**856**	**$**	**533**	**$**	**368**	**$**	**39,921**
Loans:												
Individually evaluated for impairment	$	74,783	$	46,199	$	-	$	-	$	-	$	120,982
Collectively evaluated for impairment		730,159		307,731		48,136		50,720		-		1,136,746
Total ending loans balance	**$**	**804,942**	**$**	**353,930**	**$**	**48,136**	**$**	**50,720**	**$**	**-**	**$**	**1,257,728**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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

The following tables present the activity in our allowance for loan losses and related recorded investment of the associated loans in our non-covered acquired loan portfolio, excluding loans accounted for under ASC 310-30, for the quarter and six-month period ended June 30, 2013:

	Quarter Ended June 30, 2013				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**
Allowance for loan and lease losses:					
Balance at beginning of period	$ 386	$ -	$ -	$ -	$ 386
Charge-offs	(25)	(1,158)	(1,410)	-	(2,593)
Recoveries	-	637	886	-	1,523
Provision for non-covered loan and lease losses	563	521	524	-	1,608
Balance at end of period	**$ 924**	**$ -**	**$ -**	**$ -**	**$ 924**

	Six-Month Period Ended June 30, 2013				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**
Allowance for loan and lease losses:					
Charge-offs	(25)	(2,614)	(3,125)	-	(5,764)
Recoveries	-	844	2,116	-	2,960
Provision for non-covered loan and lease losses	949	1,770	1,009	-	3,728
Balance at end of period	**$ 924**	**$ -**	**$ -**	**$ -**	**$ 924**

	June 30, 2013				
	Commercial	**Consumer**	**Auto**	**Unallocated**	**Total**

Allowance for loan and lease losses:					
Ending allowance balance attributable to loans:					
Collectively evaluated for impairment	924	-	-	-	924
Total ending allowance balance	**$ 924**	**$ -**	**$ -**	**$ -**	**$ 924**
Loans:					
Collectively evaluated for impairment	154,753	62,751	373,587	-	591,091
Total ending loan balance	**$ 154,753**	**$ 62,751**	**$ 373,587**	**$ -**	**$ 591,091**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Impaired Loans

The Company evaluates all loans, some individually and others as homogeneous groups, for purposes of determining impairment. The total investment in impaired commercial loans was $43.8 million and $46.2 million at June 30, 2013 and December 31, 2012, respectively. The impaired commercial loans were measured based on the fair value of collateral or the present value of cash flows method, including those identified as troubled-debt restructurings. The valuation allowance for impaired commercial loans amounted to approximately $5.8 million and $4.1 million at June 30, 2013 and December 31, 2012, respectively. The total investment in impaired mortgage loans was $81.8 million and $74.8 million at June 30, 2013 and December 31, 2012, respectively. Impairment on mortgage loans assessed as troubled-debt restructurings was measured using the present value of cash flows. The valuation allowance for impaired mortgage loans amounted to approximately $8.9 million and $5.3 million at June 30, 2013 and December 31, 2012, respectively.

The Company's recorded investment in commercial and mortgage loans that were individually evaluated for impairment, excluding loans accounted for under ASC 310-30, and the related allowance for loan and lease losses at June 30, 2013 and December 31, 2012 are as follows:

Originated and Other Loans and Leases Held for Investment

	June 30, 2013			
	Unpaid Principal	**Recorded Investment**	**Related Allowance**	**Coverage**
		(In thousands)		
Impaired loans with specific allowance:				
Commercial	$ 22,168	$ 19,276	$ 5,795	30%
Residential troubled-debt restructuring	85,271	81,849	8,879	11%
Impaired loans with no specific allowance:				
Commercial	31,334	24,555	N/A	N/A
Total investment in impaired loans	**$ 138,773**	**$ 125,680**	**$ 14,674**	**12%**

	December 31, 2012			
	Unpaid Principal	Recorded Investment	Related Allowance	Coverage
	(In thousands)			
Impaired loans with specific allowance				
Commercial	$ 16,666	$ 14,570	$ 4,121	28%
Residential troubled-debt restructuring	76,859	74,783	5,334	7%
Impaired loans with no specific allowance				
Commercial	36,293	31,629	N/A	N/A
Total investment in impaired loans	**$ 129,818**	**$ 120,982**	**$ 9,455**	**8%**

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

	June 30, 2013			
	Unpaid Principal	Recorded Investment	Specific Allowance	Coverage
	(In thousands)			
Impaired loans with no specific allowance				
Commercial	36,293	31,629	N/A	N/A
Total investment in impaired loans	**$ 36,293**	**$ 31,629**	**$ -**	**0%**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents the interest recognized in commercial and mortgage loans that were individually evaluated for impairment, excluding loans accounted for under ASC 310-30, for the quarters and six-month periods ended June 30, 2013 and 2012:

	Quarter Ended June 30,			
	2013		2012	
	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment
	(In thousands)			
Impaired loans with specific allowance				
Commercial	$ 255	$ 17,049	$ 132	$ 16,105
Residential troubled-debt restructuring	682	83,081	461	62,548
Impaired loans with no specific allowance				
Commercial	226	23,304	49	25,031
Total interest income from impaired loans	**$ 1,163**	**$ 123,434**	**$ 642**	**$ 103,684**

	Six-Month Period Ended June 30,			
	2013		2012	
	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment
Impaired loans with specific allowance				
Commercial	$ 322	$ 17,789	$ 264	$ 20,516
Residential troubled-debt restructuring	1,273	80,914	874	59,466
Impaired loans with no specific allowance				
Commercial	364	25,304	104	21,864
Total interest income from impaired loans	**$ 1,959**	**$ 124,007**	**$ 1,242**	**$ 101,846**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Modifications

The following table presents the troubled-debt restructurings during the quarters and six-month periods ended June 30, 2013 and 2012:

	Quarter Ended June 30, 2013						
	Number of contracts	Pre Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
	(Dollars in thousands)						
Mortgage loans	42	$ 5,372	6.47%	355	$ 5,715	4.26%	420
Commercial loans	2	1,842	8.99%	87	1,842	4.00%	66
Consumer loans	2	18	13.67%	41	18	13.67%	60

	Six-Month Period Ended June 30, 2013						
	Number of contracts	Pre Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
	(Dollars in thousands)						
Mortgage loans	86	$ 10,555	6.56%	342	$ 11,288	4.59%	417
Commercial loans	2	1,842	8.99%	87	1,842	4.00%	66
Consumer loans	2	18	13.67%	41	18	13.67%	60

	Quarter Ended June 30, 2012						
	Number of contracts	Pre Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)

	(Dollars in thousands)						
Mortgage loans	45	$ 6,028	6.52%	290	$ 6,380	4.95%	378
Commercial loans	3	3,698	6.25%	65	3,968	6.08%	71

	Six-Month Period Ended June 30, 2012						
	Number of contracts	Pre Modification Outstanding Recorded Investment	Pre-Modification Weighted Average Rate	Pre-Modification Weighted Average Term (in Months)	Post-Modification Outstanding Recorded Investment	Post-Modification Weighted Average Rate	Post-Modification Weighted Average Term (in Months)
	(Dollars in thousands)						
Mortgage loans	103	$ 15,473	6.50%	313	$ 16,419	4.96%	393
Commercial loans	6	5,600	5.80%	49	5,407	6.22%	65

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents troubled-debt restructurings for which there was a payment default during the twelve-month periods ended June 30, 2013 and 2012:

	Twelve-Month Period Ended June 30,					
	2013			2012		
	Number of Contracts	Recorded Investment		Number of Contracts	Recorded Investment	
	(Dollars in thousands)					
Mortgage loans	48	$	6,414	32	$	4,110
Consumer	2	$	29	-	$	-

Credit Quality Indicators

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

The Company uses the following definitions for risk ratings:

Special Mention: Loans classified as “special mention” have a potential weakness that deserves management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution’s credit position at some future date.

Substandard: Loans classified as “substandard” are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans classified as "doubtful" have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, questionable and improbable.

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

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

As of June 30, 2013 and December 31, 2012, and based on the most recent analysis performed, the risk category of gross non-covered originated and acquired loans accounted for under ASC 310-20 subject to risk rating by class of loans is as follows:

	June 30, 2013 Risk Ratings					
	Balance Outstanding	Pass	Special Mention	Substandard	Doubtful	Individually Measured for Impairment
	(In thousands)					
Commercial - originated and other loans held for investment						
Commercial secured by real estate	$ 412,958	$ 346,115	$ 29,355	$ 1,293	$ 282	$ 35,913
Other commercial and industrial	289,117	278,319	2,763	118	-	7,918
	702,075	624,434	32,118	1,411	282	43,831
Commercial - acquired loans (under ASC 310-20)						
Commercial secured by real estate	14,519	14,031	245	244	-	-
Other commercial and industrial	140,234	137,786	727	1,721	-	-
	154,753	151,817	972	1,965	-	-

Total	**$ 856,828**	**$ 776,251**	**$ 33,090**	**$ 3,376**	**$ 282**	**$ 43,831**

	December 31, 2012 Risk Ratings					
	Balance Outstanding	**Pass**	**Special Mention**	**Substandard**	**Doubtful**	**Individually Measured for Impairment**
	(In thousands)					
Commercial - originated and other loans held for investment						
Commercial secured by real estate	$ 251,274	$ 183,033	$ 23,928	$ 2,127	$ 99	$ 42,087
Other commercial and industrial	102,656	85,806	8,569	4,169	-	4,112
	353,930	268,839	32,497	6,296	99	46,199
Commercial - acquired loans (under ASC 310-20)						
Construction and commercial real estate	20,337	19,701	245	391	-	-
Commercial and industrial	317,632	315,085	213	2,334	-	-
	337,969	334,786	458	2,725	-	-
Total	**$ 691,899**	**$ 603,625**	**$ 32,955**	**$ 9,021**	**$ 99**	**$ 46,199**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

For residential and consumer loan classes, the Company evaluates credit quality based on the delinquency status of the loan. As of June 30, 2013 and December 31, 2012, and based on the most recent analysis performed, the risk category of non-covered gross originated loans and acquired loans accounted for under ASC 310-20 not subject to risk rating by class of loans is as follows:

	June 30, 2013							
		Delinquency						
	Balance Outstanding	0-29 days	30-59 days	60-89 days	90-119 days	120-364 days	365+ days	Individually Measured for Impairment
	(In thousands)							
Originated and other loans and leases held for investment								
Mortgage								
Traditional (by origination year)								
Up to the year 2002	$ 89,596	$ 84,184	$ -	$ 2,937	$ 367	$ 87	$ 1,719	$ 302
Years 2003 and 2004	126,596	117,665	-	5,413	1,319	737	1,373	89
Year 2005	68,763	65,026	-	2,136	663	267	502	169
Year 2006	93,821	87,259	-	3,369	968	440	1,273	512
Years 2007, 2008 and 2009	110,439	104,041	-	2,782	342	2,199	676	399
Years 2010, 2011, 2012 and 2013	98,776	94,271	-	391	951	800	365	1,998
	587,991	552,446	-	17,028	4,610	4,530	5,908	3,469
Non-traditional	46,427	42,695	-	1,520	807	160	1,152	93
Loss mitigation program	87,615	7,980	-	98	47	234	969	78,287
	722,033	603,121	-	18,646	5,464	4,924	8,029	81,849
Home equity secured	752	740	-	-	-	-	12	-

personal loans								
GNMA's buy-back option program	32,513	-	-	-	5,782	15,775	10,956	-
	755,298	603,861	-	18,646	11,246	20,699	18,997	81,849
Consumer	89,608	88,218	660	156	167	199	-	208
Auto and Leasing	233,092	221,095	8,826	2,075	759	337	-	-
	1,077,998	913,174	9,486	20,877	12,172	21,235	18,997	82,057
Acquired loans (under ASC 310-20)								
Auto	373,588	362,173	8,849	1,892	495	179	-	-
Consumer	62,751	59,908	1,767	7	1,054	15	-	-
	436,339	422,081	10,616	1,899	1,549	194	-	-
Total	**$ 1,514,337**	**$ 1,335,255**	**$ 20,102**	**$ 22,776**	**$ 13,721**	**$ 21,429**	**$ 18,997**	**$ 82,057**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

December 31, 2012		Delinquency						
	Balance Outstanding	**0-29 days**	**30-59 days**	**60-89 days**	**90-119 days**	**120-364 days**	**365+ days**	**Individually Measured for Impairment**
	(In thousands)							
Originated and other loans and leases held for investment								
Mortgage								
Traditional (by origination year):								
Up to the year 2002	$ 101,268	$ 80,715	$ 6,907	$ 2,116	$ 886	$ 3,720	$ 6,442	$ 482
Years 2003 and 2004	149,862	114,341	12,048	5,206	2,082	3,994	11,533	658
Year 2005	80,900	65,245	4,983	1,746	1,202	1,846	5,727	151
Year 2006	113,086	84,926	9,012	3,525	1,530	5,103	8,695	295
Years 2007, 2008 and 2009	121,639	108,357	2,632	1,682	641	2,532	5,732	63
Years 2010, 2011 and 2012	66,646	64,084	632	769	249	452	460	-
	633,401	517,668	36,214	15,044	6,590	17,647	38,589	1,649
Non-traditional	57,819	42,742	2,850	1,067	455	2,287	8,418	-
Loss mitigation program	87,310	9,595	606	128	102	253	3,492	73,134
	778,530	570,005	39,670	16,239	7,147	20,187	50,499	74,783
Home equity secured	736	726	-	-	-	-	10	-

personal loans								
GNMA's buy back option program	25,676	-	-	-	6,064	10,659	8,953	-
	804,942	570,731	39,670	16,239	13,211	30,846	59,462	74,783
Consumer	48,136	46,888	747	92	188	218	3	-
Auto and leasing	50,720	50,209	251	129	46	85	-	-
	903,798	667,828	40,668	16,460	13,445	31,149	59,465	74,783
Acquired loans (under ASC 310-20)								
Mortgage	1,591	1,070				521		
Auto	457,894	449,843	6,753	1,023	264	11	-	-
Consumer	68,878	66,801	982	-	1,089	4	2	-
	528,363	517,714	7,735	1,023	1,353	536	2	-
Total	**$ 1,432,161**	**$ 1,185,542**	**$ 48,403**	**$ 17,483**	**$ 14,798**	**$ 31,685**	**$ 59,467**	**$ 74,783**

The reduction in mortgage loans over 90 days past due from December 31, 2012 is due to the reclassification of certain non-performing residential mortgage loans originated before 2010, ,with the a net book value of $55.0 million to the loan held-for-sale category.

Non-covered Acquired Loans Accounted under ASC 310-30

Loans acquired in the BBVAPR Acquisition accounted for under ASC 310-30 were recognized at fair value as of December 18, 2012, which included the impact of expected credit losses, and therefore, no allowance for credit losses was recorded at the acquisition date. To the extent credit deterioration occurs after the date of acquisition, the Company would record an allowance for loan and lease losses. Management determined that there was no need to record an allowance for loan and lease losses on loans acquired in the BBVAPR Acquisition accounted for under ASC 310-30 as of June 30, 2013 and December 31, 2012.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Covered Loans

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

The changes in the allowance for loan and lease losses on covered loans for the quarters and six-month periods ended June 30, 2013 and 2012 were as follows:

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
Balance at beginning of the period	$ 52,974	$ 56,437	$ 54,124	$ 37,256
Provision for covered loan and lease losses, net	1,210	1,467	1,882	8,624
FDIC shared-loss portion of provision for (recapture of) covered loan and lease losses, net	(192)	724	(2,014)	12,748
Balance at end of the period	**$ 53,992**	**$ 58,628**	**$ 53,992**	**$ 58,628**

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

Provision for covered loans and lease losses for the quarter and six-month period ended June 30, 2013 was $1.2 million and $1.9 million, respectively, reflecting the Company’s quarterly revision of the expected cash flows in the covered loan portfolio considering actual experiences and changes in the Company’s expectations for the remaining terms of the loan pools. During the quarter ended June 30, 2013, a commercial real estate loan pool underperformed, requiring additional allowance for the quarter. The six-month period ended June 30, 2013, is mainly affected by the aforementioned commercial real estate pool together with two pools of non-performing residential mortgage loans pools. The six-month period ended June 30, 2013 was benefited by the reversal of the allowance of pools of commercial and industrial loans and pools of commercial loans secured by real estate.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company's recorded investment in covered loan pools that have recorded impairments and their related allowance for covered loan and lease losses as of June 30, 2013 and December 31, 2012 are as follows:

	June 30, 2013			
	Unpaid Principal	Recorded Investment	Specific Allowance	Coverage
		(In thousands)		
Impaired covered loan pools with specific allowance				
Loans secured by 1-4 family residential properties	$ 51,613	$ 36,483	$ 7,072	19%
Construction and development secured by 1-4 family residential properties	66,024	16,170	6,741	42%
Commercial and other construction	242,054	75,941	39,504	52%
Consumer	12,790	6,818	675	10%
Total investment in impaired covered loan pools	**$ 372,481**	**$ 135,412**	**$ 53,992**	**40%**

	December 31, 2012			
	Unpaid Principal	Recorded Investment	Specific Allowance	Coverage
		(In thousands)		
Impaired covered loan pools with specific allowance				
Loans secured by 1-4 family residential properties	$ 45,208	$ 29,482	$ 4,986	17%
Construction and development secured by 1-4 family residential properties	68,255	15,185	6,137	40%
Commercial and other construction	252,373	121,237	42,323	35%
Consumer	14,494	8,493	678	8%
Total investment in impaired covered loan pools	**$ 380,330**	**$ 174,397**	**$ 54,124**	**31%**

NOTE 6 — PREMISES AND EQUIPMENT

Premises and equipment at June 30, 2013 and December 31, 2012 are stated at cost less accumulated depreciation and amortization as follows:

	Useful Life (Years)	June 30, 2013	December 31, 2012
		(In thousands)	
Land	—	$ 5,677	$ 2,876
Buildings and improvements	40	63,673	63,133
Leasehold improvements	5 — 10	23,637	23,602
Furniture and fixtures	3 — 7	11,685	10,441
Information technology and other	3 — 7	23,271	20,874
		127,943	120,926
Less: accumulated depreciation and amortization		(43,642)	(35,929)
		$ 84,301	**$ 84,997**

Depreciation and amortization of premises and equipment totaled $3.0 million and $6.1 million in the quarter and six-month period ended June 30, 2013, respectively, and $1.2 million and $2.4 million in the quarter and six-month period ended June 30, 2012, respectively. These are included in the unaudited consolidated statements of operations as part of occupancy and equipment expenses.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 7 — DERIVATIVE ACTIVITIES

During the quarter and six-month period ended June 30, 2013, gains of $1.6 million and $1.3 million, respectively, were recognized and reflected as “Derivative Activities” in the unaudited consolidated statements of operations, which were mainly related to the mortgage hedging activities. During the quarter and six-month period ended June 30, 2012, there were no significant transactions impacting the Company’s operations reflected as “Derivative Activities” in the unaudited consolidated statements of operations.

The following table details “Derivative Assets” and “Derivative Liabilities” as reflected in the unaudited consolidated statements of financial condition at June 30, 2013 and December 31, 2012:

		June 30, 2013		December 31, 2012
		(In thousands)		
Derivative assets:				
Options tied to S&P 500 Index	$	16,020	$	13,233
Interest rate swaps not designated as hedges		3,245		8,426
Interest rate caps		270		230
Other		120		-
	$	**19,655**	**$**	**21,889**
Derivative liabilities:				
Interest rate swaps designated as cash flow hedges	$	13,187	$	17,665
Interest rate swaps not designated as hedges		3,244		8,365
Interest rate caps		270		230
	$	**16,701**	**$**	**26,260**

Interest Rate Swaps

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

The following table shows a summary of these swaps and their terms at June 30, 2013:

Type	**Notional Amount (In thousands)**	**Fixed Rate**	**Variable Rate Index**	**Trade Date**	**Settlement Date**	**Maturity Date**
Interest Rate Swaps	$ 25,000	2.4365%	1-Month Libor	05/05/11	05/04/12	05/04/16
	25,000	2.6200%	1-Month Libor	05/05/11	07/24/12	07/24/16
	25,000	2.6350%	1-Month Libor	05/05/11	07/30/12	07/30/16
	50,000	2.6590%	1-Month Libor	05/05/11	08/10/12	08/10/16
	100,000	2.6750%	1-Month Libor	05/05/11	08/16/12	08/16/16
	$ 225,000					

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

An unrealized loss of $13.2 million was recognized in accumulated other comprehensive income related to the valuation of these swaps at June 30, 2013, and the related liability is being reflected in the accompanying unaudited consolidated statements of financial condition.

At June 30, 2013 and December 31, 2012, interest rate swaps not designated as hedging instruments that were offered to clients represented an asset of $3.2 million and $8.4 million, respectively, and were included as part of derivative assets in the unaudited consolidated statements of financial position. The credit risk to these clients stemming from these derivatives, if any, is not material. At June 30, 2013 and December 31, 2012, interest rate swaps not designated as hedging instruments that are the mirror-images of the derivatives offered to clients represented a liability of $3.2 million and $8.4 million, respectively, and were included as part of derivative liabilities in the unaudited consolidated statements of financial condition.

The following table shows a summary of these interest rate swaps not designated as hedging instruments and their terms at June 30, 2013:

Type		Notional Amount (In thousands)	Fixed Rate	Variable Rate Index	Settlement Date	Maturity Date
Interest Rate Swaps - Derivatives Offered to Clients	$	4,232	5.1300%	1-Month Libor	07/03/06	07/03/16
		12,500	5.5050%	1-Month Libor	04/11/09	04/11/19
		1,150	5.1500%	3-Month Libor	10/24/08	10/24/13
	$	**17,882**				
Interest Rate Swaps - Mirror Image Derivatives	$	4,232	5.1300%	1-Month Libor	07/03/06	07/03/16
		12,500	5.5050%	1-Month Libor	04/11/09	04/11/19
		1,150	4.9550%	3-Month Libor	10/24/08	10/24/13
	$	**17,882**				

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

The Company has offered its customers certificates of deposit with an option tied to the performance of the S&P 500 Index. The Company uses option agreements with major broker-dealers to manage its exposure to changes in this index. Under the terms of the option agreements, the Company receives the average increase in the month-end value of the index in exchange for a fixed premium. The changes in fair value of the option agreements used to manage the exposure in the stock market in the certificates of deposit are recorded in earnings. At June 30, 2013 and December 31, 2012, the purchased options used to manage exposure to the S&P 500 Index on stock indexed deposits represented an asset of $16.0 million (notional amount of $49.1 million) and $13.2 million (notional amount of $66.6 million), respectively, and the options sold to customers embedded in the certificates of deposit and recorded as deposits in the unaudited consolidated statements of financial condition, represented a liability of $15.3 million (notional amount of $42.9 million) and $12.7 million (notional amount of $62.3 million), respectively.

Interest rate caps

The Company has entered into interest rate cap transactions with various clients with floating-rate debt who wish to protect their financial results against increases in interest rates. In these cases, the Company simultaneously enters into mirror-image interest rate cap transactions with financial counterparties. None of these cap transactions qualify for hedge accounting; therefore, they are marked to market through earnings. The outstanding total notional amount of interest rate caps was $94.0 million June 30, 2013 and December 31, 2012. At June 30, 2013, the interest rate caps sold to clients represented a liability of $270 thousand and were included as part of derivative liabilities in the unaudited consolidated statements of financial condition. At June 30, 2013, the interest rate caps purchased as mirror-images represented an asset of $270 thousand and were included as part of derivative assets in the unaudited consolidated statements of financial condition.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 8 — ACCRUED INTEREST RECEIVABLE AND OTHER ASSETS

Accrued interest receivable at June 30, 2013 and December 31, 2012 consists of the following:

		June 30, 2013		December 31, 2012
		(In thousands)		
Non-covered loans	$	11,459	$	10,533
Investments		6,049		7,021
	$	**17,508**	**$**	**17,554**

Other assets at June 30, 2013 and December 31, 2012 consist of the following:

		June 30, 2013		December 31, 2012
		(In thousands)		
Prepaid FDIC insurance	$	-	$	6,451
Other prepaid expenses		23,568		19,674
Servicing advances		-		7,976
Mortgage tax credits		8,706		8,706
Core deposit and customer relationship intangibles		13,201		14,490
Investment in Statutory Trust		1,086		1,086
Other repossessed assets		8,921		6,084
Accounts receivable and other assets		48,980		59,175
	$	**104,462**	**$**	**123,642**

On November 12, 2009, the FDIC adopted a final rule requiring insured depository institutions to prepay on December 31, 2009 their estimated quarterly risk-based assessments for the fourth quarter of 2009, and for all of 2010, 2011, and 2012, along with each institution's risk-based deposit insurance assessment for the third quarter of 2009. The prepayment balance of the assessment amounted to $6.5 million at December 31, 2012. Pursuant to guidelines issued by the FDIC, the assessment due for the first quarter of 2013 paid on June 28, 2013 was offset by the amount of the credit for prepaid assessments.

Other prepaid expenses amounting to $23.6 million and $19.7 million at June 30, 2013 and December 31, 2012, respectively, include prepaid municipal, property and income taxes aggregating to $17.1 million and $12.0 million, respectively.

Servicing advances amounting to $8.0 million at December 31, 2012, represent the advances made to Bayview Loan Servicing, LLC in order to service some of the loans acquired in the FDIC-assisted acquisition of Eurobank. This servicing agreement was terminated effective May 31, 2013.

At June 30, 2013 and December 31, 2012, tax credits for the Company amounted $8.7 million. Mortgage loan tax credits acquired as part of the BBVAPR Acquisition amounted to $6.3 million and $7.4 million at June 30, 2013 and December 31, 2012, respectively. These tax credits do not have an expiration date.

As part of the FDIC-assisted acquisition of Eurobank and the recent BBVAPR Acquisition, the Company recorded a core deposit intangible representing the value of checking and savings deposits acquired. At June 30, 2013 and December 31, 2012, this core deposit intangible amounted to $8.6 million and $9.5 million, respectively. In addition, as part of the BBVAPR Acquisition on December 18, 2012, the Company recorded a customer relationship intangible amounting to $5.0 million representing the value of customer relationships acquired in the broker-dealer and insurance subsidiaries as of December 31, 2012. At June 30, 2013, this customer relationship intangible amounted to $4.6 million.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Other repossessed assets totaled $8.9 million and $6.1 million at June 30, 2013 and December 31, 2012, respectively. Repossessed auto loans acquired as part of the BBVAPR Acquisition amounted to $8.6 million and $5.9 million at June 30, 2013 and December 31, 2012, respectively.

NOTE 9 — DEPOSITS AND RELATED INTEREST

Total deposits as of June 30, 2013 and December 31, 2012 consist of the following:

	June 30, 2013	December 31, 2012
	(In thousands)	
Non-interest bearing demand deposits	$ 872,806	$ 799,667
Interest-bearing savings and demand deposits	2,331,589	2,282,305
Individual retirement accounts	352,637	376,611
Retail certificates of deposit	688,877	699,983
Institutional certificates of deposits	645,037	602,828
Total core deposits	**4,890,946**	**4,761,394**
Brokered deposits	774,092	928,165
Total deposits	$ **5,665,038**	$ **5,689,559**

The weighted average interest rate of the Company's deposits was 0.73% at June 30, 2013 and 1.33% at December 31, 2012, inclusive of non-interest bearing deposits of $934.7 million and $799.7 million, respectively. Interest expense for the quarters and the six-month periods ended June 30, 2013 and 2012 was as follows:

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
Demand and savings deposits	$ 5,435	$ 2,848	$ 11,397	$ 6,024
Certificates of deposit	4,538	5,037	9,054	10,984
	$ 9,973	**$ 7,885**	**$ 20,451**	**$ 17,008**

At June 30, 2013 and December 31, 2012, demand and interest-bearing deposits and certificates of deposit included deposits of the Puerto Rico Cash & Money Market Fund Inc., which amounted to $93.3 million and $101.5 million, respectively, with a weighted average rate of 0.77% and 0.77%, and were collateralized with investment securities with a fair value of $68.3 million and $80.3 million, respectively.

At June 30, 2013 and December 31, 2012, time deposits in denominations of $100 thousand or higher, excluding accrued interest and unamortized discounts, amounted to $1.18 billion and $1.87 billion, including public fund time deposits from various Puerto Rico government municipalities, agencies, and corporations of $170.5 million and $78.3 million, respectively, at a weighted average rate of 0.48% at June 30, 2013 and 0.72% at December 31, 2012.

At June 30, 2013 and December 31, 2012, public fund deposits from various Puerto Rico government agencies were collateralized with investment securities with a fair value of $98.7 million and $114.6 million, respectively, and with commercial loans amounting to $464.1 million at June 30, 2013 and $485.8 million at December 31, 2012.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Excluding equity indexed options in the amount of $15.3 million, which are used by the Company to manage its exposure to the S&P 500 Index, and also excluding accrued interest of $3.3 million and unamortized deposit discounts in the amount of $9.0 million, the scheduled maturities of certificates of deposit at June 30, 2013 are as follows:

		June 30, 2013 (In thousands)
Within one year:		
Three (3) months or less	$	492,297
Over 3 months through 1 year		759,405
		1,251,702
Over 1 through 2 years		634,600
Over 2 through 3 years		258,143
Over 3 through 4 years		143,128
Over 4 through 5 years		61,763
	$	**2,349,336**

The aggregate amount of overdraft in demand deposit accounts that were reclassified to loans amounted to $1.0 million and $2.8 million as of June 30, 2013 and December 31, 2012, respectively.

NOTE 10 — BORROWINGS

Short term borrowings

At June 30, 2013, no short term borrowings were outstanding, compared to December 31, 2012 when these totaled $92.2 million and mainly consisted of unsecured fixed rate borrowings with a weighted average rate of 0.30%.

Securities Sold under Agreements to Repurchase

At June 30, 2013, securities underlying agreements to repurchase were delivered to, and are being held by, the counterparties with whom the repurchase agreements were transacted. The counterparties have agreed to resell to the

Company the same or similar securities at the maturity of the agreements.

At June 30, 2013 and December 31, 2012, securities sold under agreements to repurchase (classified by counterparty), excluding accrued interest in the amount of $2.3 million at both dates, were as follows:

	June 30, 2013		December 31, 2012	
	Borrowing Balance	**Fair Value of Underlying Collateral**	**Borrowing Balance**	**Fair Value of Underlying Collateral**
		(In thousands)		
UBS Financial Services Inc.	$ 500,000	$ 597,126	$ 500,000	$ 616,751
JP Morgan Chase Bank NA	255,000	273,783	412,837	443,436
Credit Suisse Securities (USA) LLC	255,000	270,180	255,000	269,943
Deutsche Bank	255,000	271,702	255,000	273,288
Citigroup Global Markets Inc.	46,573	52,473	150,000	162,652
Barclays Bank	-	-	68,650	77,521
Wells Fargo	-	-	51,444	54,943
Total	**$ 1,311,573**	**$ 1,465,264**	**$ 1,692,931**	**$ 1,898,534**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table shows a summary of the Company's repurchase agreements and their terms, excluding accrued interest in the amount of $2.3 million, at June 30, 2013:

Year of Maturity	Borrowing Balance (In thousands)		Weighted-Average Coupon	Settlement Date	Maturity Date
2013	$	46,573	0.420%	6/25/2013	7/8/2013
2014		255,000	0.500%	12/13/2012	1/7/2014
		255,000	0.550%	12/10/2012	6/13/2014
		85,000	0.675%	12/3/2012	12/3/2014
		170,000	0.675%	12/6/2012	12/8/2014
		765,000			
2017		500,000	4.665%	3/2/2007	3/2/2017
	$	**1,311,573**	**2.129%**		

None of the structured repurchase agreements referred to above with maturity dates up to the date of this report were renewed.

Advances from the Federal Home Loan Bank

Advances are received from the FHLB under an agreement whereby the Company is required to maintain a minimum amount of qualifying collateral with a fair value of at least 110% of the outstanding advances. At June 30, 2013 and December 31, 2012, these advances were secured by mortgage and commercial loans amounting to $1.3 billion both periods. Also, at June 30, 2013, the Company had an additional borrowing capacity with the FHLB of $714.4 million. At June 30, 2013 and December 31, 2012, the weighted average remaining maturity of FHLB's advances was 11.7 months and 3.5 months, respectively. The original terms of these advances range between one month and five years, and the FHLB does not have the right to exercise put options at par on any advances outstanding as of June 30, 2013.The following table shows a summary of these advances and their terms, excluding accrued interest in the amount of $294 thousand, at June 30, 2013:

Weighted-

Year of Maturity		Borrowing Balance	Average Coupon	Settlement Date	Maturity Date
		(In thousands)			
2013	$	25,000	0.360%	6/4/2013	7/5/2013
		50,000	0.360%	6/10/2013	7/10/2013
		100,000	0.390%	6/17/2013	7/16/2013
		25,000	0.400%	6/24/2013	7/24/2013
		25,000	0.410%	6/28/2013	7/30/2013
		225,000			
2017		4,844	1.240%	4/3/2012	4/3/2017
2018		30,000	2.187%	1/16/2013	1/16/2018
		25,000	2.177%	1/16/2013	1/16/2018
		55,000			
	$	**284,844**	**0.745%**		

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Subordinated Capital Notes

Subordinated capital notes amounted to $99.0 million and $146.0 million at June 30, 2013 and December 31, 2012, respectively.

In August 2003, the Statutory Trust II, a special purpose entity of the Company, was formed for the purpose of issuing trust redeemable preferred securities. In September 2003, $35.0 million of trust redeemable preferred securities were issued by the Statutory Trust II as part of a pooled underwriting transaction. Pooled underwriting involves participating with other bank holding companies in issuing the securities through a special purpose pooling vehicle created by the underwriters.

The proceeds from this issuance were used by the Statutory Trust II to purchase a like amount of a floating rate junior subordinated deferrable interest debenture issued by the Company. The subordinated deferrable interest debenture has a par value of $36.1 million, bears interest based on 3-month LIBOR plus 295 basis points (3.22% at June 30, 2013; 3.26% at December 31, 2012), is payable quarterly, and matures on September 17, 2033. It may be called at par after five years and quarterly thereafter (next call date September 2013). The trust redeemable preferred securities have the same maturity and call provisions as the subordinated deferrable interest debenture. The subordinated deferrable interest debenture issued by the Company is accounted for as a liability denominated as a subordinated capital note on the unaudited consolidated statements of financial condition.

Under Federal Reserve Board rules, restricted core capital elements, which are qualifying trust preferred securities, qualifying cumulative perpetual preferred stock (and related surplus) and certain minority interests in consolidated subsidiaries, are limited in the aggregate to no more than 25% of a bank holding company’s core capital elements (including restricted core capital elements), net of goodwill less any associated deferred tax liability. However, under the Dodd-Frank Act, and the capital rules adopted in July 2013 by the federal banking regulators to implement the agreements reached by the Basel Committee on Banking Supervision in “Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems” and to make other changes consistent with the Dodd-Frank Act, which are scheduled to become effective January 1, 2015 (subject to certain phase-in periods through January 1, 2019), bank holding companies are prohibited from including in their Tier 1 capital hybrid debt and equity securities, including trust preferred securities, issued on or after May 19, 2010. Any such instruments issued before May 19, 2010 by a bank holding company, such as the Company, with total consolidated assets of less than $15 billion as of December 31, 2009, are permanently grandfathered under the new capital rules and may continue to be included as Tier 1 capital. Therefore, the Company is permitted to continue to include its existing trust preferred securities as Tier 1 capital.

As part of the BBVAPR Acquisition on December 18, 2012, the Company's banking subsidiary assumed three subordinated capital notes issued by BBVAPR Bank consisting of the following:

- Subordinated capital notes issued in September 2004 amounting to $50.0 million at a variable rate of three-month LIBOR plus 1.44% (1.75% at December 31, 2012), that was due September 23, 2014. During the quarter ended March 31, 2013, the Bank repurchased and cancelled these subordinated capital notes in whole before maturity and realized a gain of $1.1 million in the Company's unaudited consolidated statements of operations.

- Subordinated capital notes issued in September 2006 amounting to $37.0 million at a fixed rate of 5.76% through September 29, 2011, and three-month LIBOR plus 1.56% thereafter (1.83% at June 30, 2013; 1.87% at December 31, 2012), due September 29, 2016. Interest on these subordinated notes is payable quarterly during the floating-rate period. The Bank has the option to redeem these subordinated capital notes in whole or in part from time to time before maturity at 100% of the principal amount plus any accrued but unpaid interest to the date of redemption, beginning September 29, 2011, and at each payment date thereafter.

- Subordinated capital notes issued in September 2006 amounting to $30.0 million at a variable rate of three-month LIBOR plus 1.56% thereafter (1.83% at June 30, 2013; 1.87% at December 31, 2012), due September 29, 2016. Interest on these subordinated notes is payable quarterly. The Bank has the option to redeem these subordinated capital notes in whole or in part from time to time before maturity at 100% of the principal amount plus any accrued but unpaid interest to the date of redemption, beginning September 29, 2011, and at each payment date thereafter.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

These notes qualify as Tier 2 capital at a discounted rate, which totals $40.2 million at June 30, 2013 and $50.2 million at December 31, 2012. Generally speaking, subordinated notes are included as Tier 2 capital if they have an original weighted average maturity of at least 5 years and comply with certain other requirements. As the notes approach maturity, they begin to take on characteristics of a short term obligation. For this reason, the outstanding amount eligible for inclusion in Tier 2 capital is reduced, or discounted, as the instruments approach maturity: one fifth of the outstanding amount is excluded each year during the instruments last five years before maturity. When the remaining maturity is less than one year, the instrument is excluded from Tier 2 capital.

Under the requirements of Puerto Rico Banking Act, the Bank must establish a redemption fund for the subordinated capital notes by transferring from undivided profits pre-established amounts as follows:

	Redemption fund (In thousands)	
2013	$	48,575
2014		6,700
2015		6,700
2016		5,025
	$	**67,000**

Other borrowings

Other borrowings, presented in the unaudited consolidated statements of financial condition within “Advances from FHLB and other borrowings”, amounted to $37.2 million and $17.6 million at June 30, 2013 and December 31, 2012, respectively. These borrowings mainly consists of federal funds purchased of $29.4 million and $9.9 million at June 30, 2013 and December 31, 2012, respectively, with a weighted average interest rate of 0.30% at both dates, and unsecured fixed-rate borrowings of $7.7 million at both June 30, 2013 and December 31, 2012, with a weighted average interest rate of 0.67% at both dates.

NOTE 11 — RELATED PARTY TRANSACTIONS

The Bank grants loans to its directors, executive officers and to certain related individuals or organizations in the ordinary course of business. These loans are offered at the same terms as loans to unrelated third parties. As of June 30, 2013 and December 31, 2012, these loan balances amounted to $8.0 million and $6.1 million, respectively. The activity and balance of these loans for the quarters and six-month periods ended June 30, 2013 and 2012 were as follows:

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2013	**2012**	**2013**	**2012**
	(In thousands)		**(In thousands)**	
Balance at the beginning of period	$ 8,688	$ 5,238	$ 6,055	$ 3,772
New loans	-	-	4,234	1,505
Repayments	(657)	(180)	(2,026)	(219)
Credits of persons no longer considered related parties	-	-	(232)	-
Balance at the end of period	**$ 8,031**	**$ 5,058**	**$ 8,031**	**$ 5,058**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 12 — INCOME TAXES

On June 30, 2013 the Governor signed Act No. 40 known as "Ley de Redistribución y Ajuste de la Carga Contributiva" (Act of Redistribution and Adjustment of Tax Burden). This Act, along with others signed by the Governor, comprises the budget of the Commonwealth of Puerto Rico for 2013-2014. The main purpose of the Act is to increase government collections in order to alleviate the structural deficit. The most relevant provisions of the Act, as applicable to the Company, and effective for taxable years beginning after December 31,2012 are as follows: (1) the maximum Corporate Income Tax rate was increased from 30% to 39%; (2) the allowance deduction for determining the income subject to surtax was reduced from $750,000 to $75,000 (which must be allocated among the members of a controlled group of corporations; (3) the allowable Net Operating Loss ("NOL") deduction was reduced to (i) 90% of the corporation's net income subject to regular tax, for purposes of computing the regular income tax and (ii) 80% of the alternative minimum taxable income for purposes of computing the alternative minimum tax ("AMT"); (4) the NOL carryover period was extended from 10 to 12 years for NOLs incurred after December 31, 2012; (5) a new special tax based on gross income (the "Special Tax") was added to the Puerto Rico Internal Revenue Code of 2011, as further described below; and (6) a special tax of 1% on insurance premiums earned after June 30, 2013.

In the case of non-financial institutions, the Special Tax is paid as part of the AMT and thus is accounted for under the provisions of ASC 740. The applicable rate for non-financial institutions increases gradually from 0.2% for gross income in excess of $1.0 million up to 0.85% for gross income in excess of $1.5 billion. In the case of a controlled group of corporations, the tax rate for all members of the group is determined by the aggregate gross income of all members in the group. In the case of financial institutions, the Special Tax is not part of the AMT calculation thus is accounted for as other tax not subject to the provisions of ASC 740 since the same is based on gross income. The applicable rate for financial institutions is 1%, of which fifty percent (50%) may be claimed as a credit against the financial institution's applicable income tax.

At June 30, 2013 and December 31, 2012, the Company's net deferred tax asset amounted to $155.2 million and $122.5 million, respectively. Income tax benefit for the quarter and six-month periods ended June 30, 2013 totaled $31.9 million and $24.8 million, respectively. The benefit of both periods is related to the positive effect on the deferred tax asset of the increase in the enacted tax rate from 30% to 39%. Income tax expense for the quarter and six-month period ended June 30, 2012 totaled $1.1 million and $3.0 million, respectively.

At June 30, 2013 and December 31, 2012, OIB had $415 thousand and $504 thousand, respectively, in the income tax effect of unrecognized gain on available-for-sale securities included in other comprehensive income. Following the change in OIB's applicable tax rate from 5% to 0% as a result of a Puerto Rico law adopted in 2011, this remaining tax balance will flow through income as these securities are repaid or sold in future periods. During the quarters ended June 30, 2013 and 2012, $43 thousand and $166 thousand, respectively, related to this residual tax effect from OIB was reclassified from accumulated other comprehensive income into income tax provision. During the six-month periods ended June 30, 2013 and 2012, $89 thousand and $724 thousand, respectively, related to this residual effect from OIB was reclassified from accumulated other comprehensive income to income tax provision.

The Company maintained an effective tax rate for the six-month period ended June 30, 2013 lower than the new maximum marginal statutory rate of 39.00%. The reconciliation of the enacted tax rate and the effective income tax rate for the six-month period ended June 30, 2013 follows:

	Six-Month Period Ended June 30, 2013		
	Amount		Rate
	(Dollars in thousands)		
Tax at statutory rates	$	13,230	39.00%
Tax effect of exempt income, net		(3,607)	-10.63%
Effect in deferred taxes due to increase in tax rates from 30.00% to 39.00%		(36,928)	-108.85%
Other items, net		2,497	7.35%
Income tax benefit	**$**	**(24,808)**	**-73.13%**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company classifies unrecognized tax benefits in income taxes payable. These gross unrecognized tax benefits would affect the effective tax rate if realized. The balance of unrecognized tax benefits at June 30, 2013 was $5.6 million (December 31, 2012 - $5.3 million). The Company had accrued $1.7 million at June 30, 2013 (December 31, 2012 - $1.4 million) for the payment of interest and penalties relating to unrecognized tax benefits. As part of the BBVAPR Acquisition, there are unrecognized tax benefits amounting to $3.9 million at June 30, 2013 and December 31, 2012. There is also $812 thousand (December 31, 2012 - $665 thousand) in accrued payment of interest and penalties relating to unrecognized tax benefits.

NOTE 13 — STOCKHOLDERS' EQUITY AND EARNINGS PER COMMON SHARE

Regulatory Capital Requirements

The Company (on a consolidated basis) and the Bank are subject to various regulatory capital requirements administered by federal and Puerto Rico banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Pursuant to the Dodd-Frank Act, federal banking regulators have adopted new capital rules that are scheduled to become effective January 1, 2015 (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.

Quantitative measures established by regulation to ensure capital adequacy currently require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined in the regulations) and of Tier 1 capital to average assets (as defined in the regulations). As of June 30, 2013 and December 31, 2012, the Company and the Bank met all capital adequacy requirements to which they are subject. As of June 30, 2013 and December 31, 2012, the Bank is "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," an institution must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following tables.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The Company's and the Bank's actual capital amounts and ratios as of June 30, 2013 and December 31, 2012 are as follows:

	Actual		Minimum Capital Requirement	
	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)			
Company Ratios				
As of June 30, 2013				
Total capital to risk-weighted assets	$ 807,190	**15.83%**	$ 407,818	**8.00%**
Tier 1 capital to risk-weighted assets	$ 702,801	**13.79%**	$ 203,909	**4.00%**
Tier 1 capital to total assets	$ 702,801	**8.54%**	$ 329,223	**4.00%**
As of December 31, 2012				
Total capital to risk-weighted assets	$ 794,195	**15.15%**	$ 419,269	**8.00%**
Tier 1 capital to risk-weighted assets	$ 678,127	**12.94%**	$ 209,634	**4.00%**
Tier 1 capital to total assets	$ 678,127	**6.42%**	$ 422,307	**4.00%**

	Actual		Minimum Capital Requirement		Minimum to be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)					
Bank Ratios						
As of June 30, 2013						
Total capital to risk-weighted assets	$ 743,653	**15.01%**	$ 396,291	**8.00%**	$ 495,363	**10.00%**
Tier 1 capital to risk-weighted assets	$ 641,043	**12.94%**	$ 198,145	**4.00%**	$ 297,218	**6.00%**
Tier 1 capital to total assets	$ 641,043	**7.84%**	$ 327,058	**4.00%**	$ 408,823	**5.00%**
As of December 31, 2012						
Total capital to risk-weighted assets	$ 719,675	**14.03%**	$ 410,268	**8.00%**	$ 512,835	**10.00%**
Tier 1 capital to risk-weighted assets	$ 604,997	**11.80%**	$ 205,134	**4.00%**	$ 307,701	**6.00%**
Tier 1 capital to total assets	$ 604,997	**5.76%**	$ 420,298	**4.00%**	$ 525,373	**5.00%**

Additional paid-in capital

Additional paid-in capital represents contributed capital in excess of par value of common and preferred stock net of costs of the issuance. As of June 30, 2013, accumulated issuance costs charged against additional paid in capital amounted to $10.1 million and $13.6 million for preferred and common stock, respectively.

Legal Surplus

The Puerto Rico Banking Act requires that a minimum of 10% of the Bank's net income for the year be transferred to a reserve fund until such fund (legal surplus) equals the total paid in capital on common and preferred stock. At June 30, 2013 and December 31, 2012, the Bank's legal surplus amounted to $57.9 million and $52.1 million, respectively. The amount transferred to the legal surplus account is not available for the payment of dividends to shareholders.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Earnings per Common Share

The calculation of earnings per common share for the quarters and six-month periods ended June 30, 2013 and 2012 is as follows:

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2013	**2012**	**2013**	**2012**
	(In thousands, except per share data)			
Net income	$ 37,539	$ 14,958	$ 58,731	$ 25,610
Less: Dividends on preferred stock				
Non-Convertible Preferred Stock (Series A, B, and D)	(1,629)	(1,201)	(3,256)	(2,401)
Convertible preferred stock (Series C)	(1,837)	-	(3,675)	-
Income available to common shareholders	**$ 34,073**	**$ 13,757**	**$ 51,800**	**$ 23,209**
Effect of assumed conversion of the Convertible Preferred Stock	1,837	**-**	3,675	**-**
Income available to common shareholders assuming conversion	$ **35,910**	$ **13,757**	$ **55,475**	$ **23,209**
Weighted average common shares and share equivalents:				
Average common shares outstanding	45,630	40,703	45,613	40,873
Effect of dilutive securities:				
Average potential common shares-options	200	105	178	113
Average potential common shares-assuming conversion of convertible preferred stock	7,138	**-**	7,138	-
Total weighted average common shares outstanding and equivalents	**52,968**	**40,808**	**52,929**	**40,986**
Earnings per common share - basic	**$ 0.75**	**$ 0.34**	**$ 1.14**	**$ 0.57**
Earnings per common share - diluted	**$ 0.68**	**$ 0.34**	**$ 1.05**	**$ 0.57**

In computing diluted earnings per common share, the 84,000 shares of convertible preferred stock, which remained outstanding at June 30, 2013, with a conversion rate, subject to certain conditions, of 84.9798 shares of common stock per share, were included as average potential common shares from the date they were issued and outstanding. Moreover, in computing diluted earnings per common share, the dividends declared during the quarter and six-month period ended June 30, 2013 on the convertible preferred stock were added back as income available to common shareholders.

For the quarters ended June 30, 2013 and 2012, weighted-average stock options with an anti-dilutive effect on earnings per share not included in the calculation amounted to 243,721 and 708,976, respectively. For the six-month periods ended June 30, 2013 and 2012, weighted-average stock options with an anti-dilutive effect on earnings per share not included in the calculation amounted to 578,393 and 707,143, respectively.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Treasury Stock

Repurchased common stock is held by the Company as treasury shares. The Company records treasury stock purchases under the cost method whereby the entire cost of the acquired stock is recorded as treasury stock.

The activity in connection with common shares held in treasury by the Company for the six-month periods ended June 30, 2013 and 2012 is set forth below:

	Six-Month Period Ended June 30,			
	2013		2012	
	Shares	Dollar Amount	Shares	Dollar Amount
	(In thousands, except shares data)			
Beginning of period	7,090,597	$ 81,275	6,564,124	$ 74,808
Common shares used upon lapse of restricted stock units	(34,800)	(364)	(37,446)	(392)
Common shares repurchased as part of the stock repurchase program	-	-	603,000	7,022
Common shares used to match defined contribution plan, net	(7,318)	(77)	(18,898)	(35)
End of period	**7,048,479**	**$ 80,834**	**7,110,780**	**$ 81,403**

Accumulated Other Comprehensive Income

Accumulated other comprehensive income, net of income tax, as of June 30, 2013 and December 31, 2012 consisted of:

	June 30, 2013	December 31, 2012
	(In thousands)	
Unrealized gain on securities available-for-sale which are not	$ 28,779	$ 75,347

other-than-temporarily impaired				
Income tax effect of unrealized gain on securities available-for-sale		(3,379)		(7,102)
Net unrealized gain on securities available-for-sale which are not other-than-temporarily impaired		25,400		68,245
Unrealized loss on cash flow hedges		(13,187)		(17,664)
Income tax effect of unrealized loss on cash flow hedges		3,553		5,299
Net unrealized loss on cash flow hedges		(9,634)		(12,365)
	$	**15,766**	**$**	**55,880**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents changes in accumulated other comprehensive income by component, net of taxes, for the quarter and the six-month period ended June 30, 2013:

	Quarter Ended June 30, 2013			Six-Month Period Ended June 30, 2013		
	Net unrealized gains on securities available-for-sale	Net unrealized loss on cash flow hedges	Accumulated other comprehensive income	Net unrealized gains on securities available-for-sale	Net unrealized loss on cash flow hedges	Accumulated other comprehensive income
	(In thousands)			(In thousands)		
Beginning balance	$ 58,393	$ (11,342)	$ 47,051	$ 68,245	$ (12,365)	$ 55,880
Other comprehensive income before reclassifications	(33,036)	292	(32,744)	(42,934)	(21)	(42,955)
Amounts reclassified out of accumulated other comprehensive income	43	1,416	1,459	89	2,752	2,841
Other comprehensive income (loss)	(32,993)	1,708	(31,285)	(42,845)	2,731	(40,114)
Ending balance	**$ 25,400**	**$ (9,634)**	**$ 15,766**	**$ 25,400**	**$ (9,634)**	**$ 15,766**

The following table presents reclassifications out of accumulated other comprehensive income for the quarter and six-month period ended June 30, 2013:

	Quarter Ended June 30, 2013	Six-Month Period Ended June 30, 2013	Affected Line Item in Consolidated Statement of Operations
	(In thousands)	(In thousands)	
Cash flow hedges:			
Interest-rate contracts	$ 1,416	$ 2,752	Net interest expense
Available-for-sale securities:			

Residual tax effect from OIB's change in applicable tax rate	43	89	Income tax expense
	$ 1,459	**$ 2,841**	

At June 30, 2013 and December 31, 2012, OIB had $415 thousand and $504 thousand, respectively, in the income tax effect of unrecognized gain on available-for-sale securities included in other comprehensive income. Following the change in OIB’s applicable tax rate from 5% to 0% as a result of a new Puerto Rico law adopted in 2011, this remaining tax balance will flow through income as these securities are repaid or sold in future periods.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 14 — COMMITMENTS

Loan Commitments

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

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

Summarized credit-related financial instruments at June 30, 2013 and December 31, 2012 were as follows:

	June 30, 2013	December 31, 2012
	(In thousands)	
Commitments to extend credit	$ 445,411	$ 591,679
Commercial letters of credit	2,231	2,918

Commitments from loans acquired as part of the BBVAPR Acquisition amounted to $337.1 million and $461.6 million at June 30, 2013 and December 31, 2012, respectively. Commitments to extend credit represent agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Company upon the extension of credit, is based on management's credit evaluation of the counterparty.

At June 30, 2013 and December 31, 2012, commitments to extend credit consisted mainly of undisbursed available amounts on commercial lines of credit, construction loans, and revolving credit card arrangements. Since many of the unused commitments are expected to expire unused or be only partially used, the total amount of these unused commitments does not necessarily represent future cash requirements. These lines of credit had a reserve of $900 thousand at both June 30, 2013 and December 31, 2012.

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The summary of instruments that are considered financial guarantees in accordance with the authoritative guidance related to guarantor's accounting and disclosure requirements for guarantees, including indirect guarantees of indebtedness of others, at June 30, 2013 and December 31, 2012, is as follows:

	June 30, 2013	December 31, 2012
	(In thousands)	
Standby letters of credit and financial guarantees	$ 67,087	$ 69,789
Loans sold with recourse	184,937	172,492
Commitments to sell or securitize mortgage loans	10,977	83,663

Standby letters of credit and financial guarantees are written conditional commitments issued by the Company to guarantee the payment and/or performance of a customer to a third party ("beneficiary"). If the customer fails to comply with the agreement, the beneficiary may draw on the standby letter of credit or financial guarantee as a remedy. The amount of credit risk involved in issuing letters of credit in the event of nonperformance is the face amount of the letter of credit or financial guarantee. These guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing, and similar transactions. The amount of collateral obtained, if it is deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the customer. The Company does not expect any significant losses under these obligations. As of June 30, 2013 and December 31, 2012, no performance was required on any financial guarantees. As part of the BBVAPR Acquisition, the Company assumed $65.9 million of standby letters of credit and $169.3 million of loans sold without recourse commitments at December 31, 2012.

Lease Commitments

The Company has entered into various operating lease agreements for branch facilities and administrative offices. Rent expense for the quarters ended June 30, 2013 and 2012 amounted to $2.6 million and $1.6 million, respectively, and is included in the "occupancy and equipment" caption in the unaudited consolidated statements of operations. For the six-month periods ended June 30, 2013 and 2012, rent expense amounted to $5.2 million and $3.3 million, respectively. Future rental commitments under leases in effect at June 30, 2013, exclusive of taxes, insurance, and maintenance expenses payable by the Company, are summarized as follows:

Year Ending June 30,	Minimum Rent (In thousands)

2013	$	5,332
2014		8,402
2015		8,116
2016		7,492
2017		7,965
Thereafter		24,755
	$	**62,062**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

NOTE 15 — CONTINGENCIES

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

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

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

NOTE 16 - FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company follows the fair value measurement framework under GAAP.

Fair Value Measurement

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

Money market investments

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

Investment securities

The fair value of investment securities is based on quoted market prices, when available, or market prices provided by recognized broker-dealers. If listed prices or quotes are not available, fair value is based upon externally developed models that use both observable and unobservable inputs depending on the market activity of the instrument. The Company holds two securities categorized as other debt that are classified as Level 3. The estimated fair value of the other debt securities is determined by using a third-party model to calculate the present value of projected future cash flows. The assumptions are highly uncertain and include primarily market discount rates, current spreads, and an indicative pricing. The assumptions used are drawn from similar securities that are actively traded in the market and have similar characteristics as the collateral underlying the debt securities being evaluated. The valuation is performed on a monthly basis.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Derivative instruments

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

Certain other derivative instruments with limited market activity are valued using externally developed models that consider unobservable market parameters. Based on their valuation methodology, derivative instruments are classified as Level 2 or Level 3. The Company has offered its customers certificates of deposit with an option tied to the performance of the S&P Index and uses equity indexed option agreements with major broker-dealers to manage its exposure to changes in this index. Their fair value is obtained through the use of an external based valuation that was thoroughly evaluated and adopted by management as its measurement tool for these options. The payoff of these options is linked to the average value of the S&P Index on a specific set of dates during the life of the option. The methodology uses an average rate option or a cash-settled option whose payoff is based on the difference between the expected average value of the S&P Index during the remaining life of the option and the strike price at inception. The assumptions, which are uncertain and require a degree of judgment, include primarily S&P Index volatility, forward interest rate projections, estimated index dividend payout, and leverage.

Servicing assets

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

Loans receivable considered impaired that are collateral dependent

The impairment is measured based on the fair value of the collateral, which is derived from appraisals that take into consideration prices in observed transactions involving similar assets in similar locations, in accordance with the provisions of ASC 310-10-35. Currently, the associated loans considered impaired are classified as Level 3.

Foreclosed real estate

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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

	June 30, 2013 Fair Value Measurements			
	Level 1	**Level 2**	**Level 3**	**Total**
		(In thousands)		
Recurring fair value measurements:				
Investment securities available-for-sale	$ -	$ 1,816,172	$ 20,057	$ 1,836,229
Money market investments	10,983	-	-	10,983
Derivative assets	-	3,635	16,020	19,655
Servicing assets	-	-	12,994	12,994
Derivative liabilities	-	(16,701)	(15,315)	(32,016)
	$ 10,983	**$ 1,803,106**	**$ 33,756**	**$ 1,847,845**
Non-recurring fair value measurements:				
Impaired commercial loans	$ -	$ -	$ 43,831	$ 43,831
Foreclosed real estate	-	-	81,689	81,689
	$ -	**$ -**	**$ 125,520**	**$ 125,520**

	December 31, 2012 Fair Value Measurements			
	Level 1	**Level 2**	**Level 3**	**Total**
		(In thousands)		
Recurring fair value measurements:				
Investment securities available-for-sale	$ -	$ 2,174,274	$ 20,012	$ 2,194,286
Securities purchased under agreements to resell	-	80,000	-	80,000
Money market investments	13,205	-	-	13,205
Derivative assets	-	8,656	13,233	21,889
Servicing assets	-	-	10,795	10,795
Derivative liabilities	-	(26,260)	(12,707)	(38,967)
	$ 13,205	**$ 2,236,670**	**$ 31,333**	**$ 2,281,208**
Non-recurring fair value measurements:				
Impaired commercial loans	$ -	$ -	$ 46,199	$ 46,199
Foreclosed real estate	-	-	75,447	75,447
	$ -	**$ -**	**$ 121,646**	**$ 121,646**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The table below presents a reconciliation of all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the quarters and the six-month periods ended June 30, 2013 and 2012:

	Quarter Ended June 30, 2013				
Level 3 Instruments Only	**Other debt securities available-for-sale**	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
Balance at beginning of period	$ 20,042	$ 15,404	$ 11,543	$ (14,839)	$ 32,150
Gains (losses) included in earnings	-	616	-	(516)	100
Changes in fair value of investment securities available for sale included in other comprehensive income	16	-	-	-	16
New instruments acquired	-	-	1,301	-	1,301
Principal repayments	-	-	(489)	-	(489)
Amortization	-	-	-	40	40
Changes in fair value of servicing assets	-	-	639	-	639
Balance at end of period	**$ 20,058**	**$ 16,020**	**$ 12,994**	**$ (15,315)**	**$ 33,757**

	Quarter Ended June 30, 2012					
	Investment securities available-for-sale					
Level 3 Instruments Only	**CLOs**	**Other debt securities**	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
	$ 29,643	$ 9,882	$ 12,515	$ 10,725	$ (12,138)	$ 50,627

Balance at beginning of period						
Gains (losses) included in earnings	-	-	(1,148)	-	1,119	(29)
Changes in fair value of investment securities available for sale included in other comprehensive income	(2,381)	134	-	-	-	(2,247)
New instruments acquired	-	-	-	499	-	499
Principal repayments	18	-	-	(241)	-	(223)
Amortization	-	-	-	-	107	107
Changes in fair value of servicing assets	-	-	-	(207)	-	(207)
Balance at end of period	$ **27,280**	$ **10,016**	$ **11,367**	$ **10,776**	$ **(10,912)**	$ **48,527**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Six-Month Period Ended June 30, 2013				
Level 3 Instruments Only	**Other debt securities available-for-sale**	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
Balance at beginning of period	$ 20,012	$ 13,233	$ 10,795	$ (12,707)	$ 31,333
Gains (losses) included in earnings	-	2,787	-	(2,923)	(136)
Changes in fair value of investment securities available for sale included in other comprehensive income	46	-	-	-	46
New instruments acquired	-	-	1,994	-	1,994
Principal repayments	-	-	(557)	-	(557)
Amortization	-	-	-	315	315
Changes in fair value of servicing assets	-	-	762	-	762
Balance at end of period	**$ 20,058**	**$ 16,020**	**$ 12,994**	**$ (15,315)**	**$ 33,757**

	Six-Month Period Ended June 30, 2012						
	Investment securities available-for-sale						
Level 3 Instruments Only	**CDOs**	**CLOs**	**Other debt securities**	**Derivative asset (S&P Purchased Options)**	**Servicing assets**	**Derivative liability (S&P Embedded Options)**	**Total**
			(In thousands)				
Balance at beginning of period	$ 10,530	$ 26,758	$ 10,024	$ 9,317	$ 10,454	$ (9,362)	$ 57,721
Gains (losses) included in earnings	-	-	-	2,050	-	(2,035)	15

Changes in fair value of investment securities available for sale included in other comprehensive income	-	488	(7)	-	-	-	481
New instruments acquired	-	-	-	-	919	-	919
Principal repayments	-	34	-	-	(476)	-	(442)
Amortization	-	-	(1)	-	-	485	484
Sales of instruments	(10,530)	-	-	-	-	-	(10,530)
Changes in fair value of servicing assets	-	-	-	-	(121)	-	(121)
Balance at end of period	$ **-**	$ **27,280**	$ **10,016**	$ **11,367**	$ **10,776**	$ **(10,912)**	$ **48,527**

During the quarters and the six-month periods ended June 30, 2013 and 2012, there were purchases and sales of assets and liabilities measured at fair value on a recurring basis. There were no transfers into and out of Level 1 and Level 2 fair value measurements during such periods.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The table below presents quantitative information for all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) at June 30, 2013:

		June 30, 2013		
	Fair Value (In thousands)	Valuation Technique	Unobservable Input	Range
Investment securities available-for-sale: Other debt securities	$ 20,058	Market comparable bonds	Indicative pricing	97.50% - 100.50%
			Option adjusted spread	289.1% - 469.2%
			Yield to maturity	3.060% - 5.101%
			Spread to maturity	288.7% - 470.2%
Derivative assets (S&P Purchased Options)	$ 16,020	Option pricing model	Implied option volatility	24.82% - 39.16%
			Counterparty credit risk (based on 5-year credit default swap ("CDS") spread)	100.28% - 174.12%
Servicing assets	$ 12,994	Cash flow valuation	Constant prepayment rate	8.41% - 26.96%
			Discount rate	10.50% - 13.50%
Derivative liability (S&P	$ (15,315)	Option pricing model	Implied option volatility	24.82% - 39.16%

Embedded Options)					
				Counterparty credit risk (based on 5-year CDS spread)	100.28% - 174.12%
Collateral dependant impaired loans	$	43,831	Fair value of property or collateral	Appraised value	Not meaningful

Information about Sensitivity to Changes in Significant Unobservable Inputs

Other debt securities – The significant unobservable inputs used in the fair value measurement of one of the Company's other debt securities are indicative comparable pricing, option adjusted spread ("OAS"), yield to maturity, and spread to maturity. Significant changes in any of those inputs in isolation would result in a significantly different fair value measurement. Generally, a change in the assumption used for indicative comparable pricing is accompanied by a directionally opposite change in the assumption used for OAS and a directionally, although not equally proportional, opposite change in the assumptions used for yield to maturity and spread to maturity.

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

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

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

The table below presents a detail of investment securities available-for-sale classified as Level 3 at June 30, 2013:

	June 30, 2013				
Type	**Amortized Cost**	**Unrealized Gains (Losses)**	**Fair Value**	**Weighted Average Yield**	**Principal Protection**
	(In thousands)				
Other debt securities	**$ 20,000**	**$ 58**	**$ 20,058**	**3.50%**	N/A

Fair Value of Financial Instruments

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

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

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The estimated fair value and carrying value of the Company's financial instruments at June 30, 2013 and December 31, 2012 is as follows:

	June 30, 2013		December 31, 2012	
	Fair Value	Carrying Value	Fair Value	Carrying Value
		(In thousands)		
Level 1				
Financial Assets:				
Cash and cash equivalents	$ 748,313	$ 748,313	$ 868,695	$ 868,695
Level 2				
Financial Assets:				
Securities purchased under agreements to resell	-	-	80,000	80,000
Securities sold but not yet delivered	16,732	16,732	-	-
Trading securities	2,209	2,209	495	495
Investment securities available-for-sale	1,816,171	1,816,171	2,174,274	2,174,274
Federal Home Loan Bank (FHLB) stock	22,156	22,156	38,411	38,411
Derivative assets	3,635	3,635	8,656	8,656
Financial Liabilities:				
Derivative liabilities	16,701	16,701	26,260	26,260
Short term borrowings	-	-	92,210	92,210
Level 3				
Financial Assets:				
Investment securities available-for-sale	20,058	20,058	20,012	20,012
Total loans (including loans held-for-sale)				
Non-covered loans, net	4,600,628	4,621,649	4,766,179	4,773,923
Covered loans, net	449,113	369,380	489,885	395,307
Derivative assets	16,020	16,020	13,233	13,233
FDIC shared-loss indemnification asset	173,442	236,472	204,646	286,799
Accrued interest receivable	17,508	17,508	17,554	17,554
Servicing assets	12,994	12,994	10,795	10,795
Financial Liabilities:				
Deposits	5,688,574	5,665,038	5,797,097	5,689,559
	1,353,970	1,313,870	1,741,272	1,695,247

Securities sold under agreements to repurchase				
Advances from FHLB	283,443	285,135	538,355	536,542
Federal funds purchased	29,431	29,431	9,901	9,901
Term notes	7,710	7,734	7,912	7,734
Subordinated capital notes	98,008	98,961	146,415	146,038
Accrued expenses and other liabilities	117,569	117,569	102,169	102,169

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following methods and assumptions were used to estimate the fair values of significant financial instruments at June 30, 2013 and December 31, 2012:

- Cash and cash equivalents (including money market investments and time deposits with other banks), accrued interest receivable, securities purchased under agreements to resell, securities sold but not yet delivered, accrued expenses and other liabilities have been valued at the carrying amounts reflected in the unaudited consolidated statements of financial condition as these are reasonable estimates of fair value given the short-term nature of the instruments.

- Investments in FHLB stock are valued at their redemption value.

- The fair value of investment securities, including trading securities, is based on quoted market prices, when available, or market prices provided by recognized broker-dealers. If listed prices or quotes are not available, fair value is based upon externally developed models that use both observable and unobservable inputs depending on the market activity of the instrument. The estimated fair value of the structured credit investments is determined by using a third-party cash flow valuation model to calculate the present value of projected future cash flows. The assumptions used which are highly uncertain and require a high degree of judgment, include primarily market discount rates, current spreads, duration, leverage, default, home price depreciation, and loss rates. The assumptions used are drawn from a wide array of data sources, including the performance of the collateral underlying each deal. The external-based valuation, which is obtained at least on a quarterly basis, is analyzed and its assumptions are evaluated and incorporated in either an internal-based valuation model when deemed necessary, or compared to counterparties' prices and agreed by management.

- The fair value of the FDIC shared-loss indemnification asset represents the present value of the estimated cash payments (net of amounts owed to the FDIC) expected to be received from the FDIC for future losses on covered assets based on the credit assumptions on estimated cash flows for each covered asset pool and the loss sharing percentages. The ultimate collectability of the FDIC shared-loss indemnification asset is dependent upon the performance of the underlying covered loans, the passage of time and claims paid by the FDIC which are impacted by the Bank's adherence to certain guidelines established by the FDIC.

- The fair value of servicing assets is estimated by using a cash flow valuation model which calculates the present value of estimated future net servicing cash flows, taking into consideration actual and expected loan prepayment rates, discount rates, servicing costs, and other economic factors, which are determined based on current market conditions.

• The fair values of the derivative instruments are provided by valuation experts and counterparties. Certain derivatives with limited market activity are valued using externally developed models that consider unobservable market parameters. The Company has offered its customers certificates of deposit with an option tied to the performance of the S&P Index, and uses equity indexed option agreements with major broker-dealers to manage its exposure to changes in this index. Their fair value is obtained through the use of an external based valuation that was thoroughly evaluated and adopted by management as its measurement tool for these options. The payoff of these options is linked to the average value of the S&P Index on a specific set of dates during the life of the option. The methodology uses an average rate option or a cash-settled option whose payoff is based on the difference between the expected average value of the S&P Index during the remaining life of the option and the strike price at inception. The assumptions, which are uncertain and require a degree of judgment, include primarily S&P Index volatility, forward interest rate projections, estimated index dividend payout, and leverage.

• Fair value of derivative liabilities, which include interest rate swaps and forward-settlement swaps, are based on the net discounted value of the contractual projected cash flows of both the pay-fixed receive-variable legs of the contracts. The projected cash flows are based on the forward yield curve, and discounted using current estimated market rates.

• The fair value of the covered and non-covered loan portfolio (including loans held-for-sale) is estimated by segregating by type, such as mortgage, commercial, consumer, and leasing. Each loan segment is further segmented into fixed and adjustable interest rates and by performing and non-performing categories. The fair value of performing loans is calculated by discounting contractual cash flows, adjusted for prepayment estimates (voluntary and involuntary), if any, using estimated current market discount rates that reflect the credit and interest rate risk inherent in the loan. This fair value is not currently an indication of an exit price as that type of assumption could result in a different fair value estimate.

• The fair value of demand deposits and savings accounts is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is based on the discounted value of the contractual cash flows, using estimated current market discount rates for deposits of similar remaining maturities.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

- For short term borrowings and federal funds purchased, the carrying amount is considered a reasonable estimate of fair value. The fair value of long-term borrowings, which include securities sold under agreements to repurchase, advances from FHLB, FDIC-guaranteed term notes, other term notes, and subordinated capital notes, is based on the discounted value of the contractual cash flows using current estimated market discount rates for borrowings with similar terms, remaining maturities and put dates.

- The fair value of commitments to extend credit and unused lines of credit is based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standings.

NOTE 17 — OFFSETTING ARRANGEMENTS

The Company manages credit and counterparty risk by entering into enforceable netting agreements and other collateral arrangements with counterparties to derivative financial instruments and secured financing transactions, including resale and repurchase agreements, and principal securities borrowing and lending agreements. These netting agreements mitigate counterparty credit risk by providing for a single net settlement with a counterparty of all financial transactions covered by the agreement in an event of default as defined under such agreement. In limited cases, a netting agreement may also provide for the periodic netting of settlement payments with respect to multiple different transaction types in the normal course of business.

Certain of the Company derivative contracts are executed under either standardized netting agreements or, for exchange-traded derivatives, the relevant contracts for a particular exchange which contain enforceable netting provisions. In certain cases, the Company may have cross-product netting arrangements which allow for netting and set-off of a variety of types of derivatives with a single counterparty. A derivative netting arrangement creates an enforceable right of set-off that becomes effective, and affects the realization or settlement of individual financial assets and liabilities, only following a specified event of default. Collateral requirements associated with the derivative contracts are determined after a review of the creditworthiness of each counterparty, and the requirements are monitored and adjusted daily, typically based on net exposure by counterparty. Collateral is generally in the form of cash or highly liquid U.S. government securities.

In connection with the Company's secured financing activities, the Company enters into netting agreements and other collateral arrangements with counterparties, which provide for the right to liquidate collateral upon an event of default. Required collateral is generally in the form of cash, equities or fixed-income securities. Default events may include the failure to timely make payments or deliver securities, material adverse changes in financial condition or insolvency, the breach of minimum regulatory capital requirements, or loss of license, charter or other legal authorization necessary to perform under the contract.

In order for an arrangement to be eligible for netting, the Company must have a basis to conclude that such netting arrangements are legally enforceable. The analysis of the legal enforceability of an arrangement differs by jurisdiction, depending on the laws of that jurisdiction. In many jurisdictions, specific legislation exists that provides for the enforceability in bankruptcy of close-out netting under a netting agreement, typically by way of specific exception from more general prohibitions on the exercise of creditor rights.

Even though the Company has enforceable netting arrangements, they do not meet the applicable offsetting criteria, and therefore are not offset in the unaudited consolidated statements of financial condition. In addition, the Company does not offset secured financing assets and liabilities.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents derivative financial instruments and secured financing transactions that are subject to enforceable netting arrangements, but do not meet the applicable offsetting criteria and therefore were not offset in our unaudited consolidated statements of financial condition, as of the dates indicated:

	June 30, 2013			
	Net amount of Assets Presented in Statement of Financial Condition	Financial Instruments	Cash Collateral Received	Net Amount
	(In thousands)			
Derivatives	$ 19,655	$ -	$ -	$ 19,655
Total	**$ 19,655**	**$ -**	**$ -**	**$ 19,655**

	December 31, 2012			
	Net amount of Assets Presented in Statement of Financial Condition	Financial Instruments	Cash Collateral Received	Net Amount
	(In thousands)			
Derivatives	$ 21,889	$ -	$ -	$ 21,889
Resale agreements and securities borrowings (1)	80,000	-	-	80,000
Total	**$ 101,889**	**$ -**	**$ -**	**$ 101,889**

(1) Excludes the impact of non-cash collateral. These secured financing transactions are fully collateralized.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

The following table presents derivative financial instruments and secured financing transactions subject to enforceable netting arrangements that do not meet the applicable offsetting criteria and therefore were not offset in our unaudited consolidated statements of financial condition, as of the dates indicated:

	June 30, 2013							
	Net amount of Liabilities Presented in Statement of Financial Condition			Financial Instruments		Cash Collateral Provided		Net Amount
	(In thousands)							
Derivatives	$	19,534	$	-	$	-	$	19,534
Repurchase agreements and securities lending (1)		1,311,573		-		-		1,311,573
Total	**$**	**1,331,107**	**$**	**-**	**$**	**-**	**$**	**1,331,107**

	December 31, 2012							
	Net amount of Liabilities Presented in Statement of Financial Condition			Financial Instruments		Cash Collateral Provided		Net Amount
	(In thousands)							
Derivatives	$	21,302	$	-	$	-	$	21,302
Repurchase agreements and securities lending (1)		1,692,931		-		-		1,692,931
Total	**$**	**1,714,233**	**$**	**-**	**$**	**-**	**$**	**1,714,233**

(1) Excludes the impact of non-cash collateral. These secured financing transactions are fully collateralized.

NOTE 18 – BUSINESS SEGMENTS

The Company segregates its businesses into the following major reportable segments of business: Banking, Financial Services, 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 organization, nature of its 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 goals of different financial parameters such as net income, net interest income, loan production, and fees generated. The Company's methodology for allocating non-interest expenses among segments is based on several factors such as revenue, employee headcount, occupied space, dedicated services or time, among others. These factors are reviewed on a periodical basis and may change if the conditions warrant.

Banking includes the Bank's branches and traditional banking products such as deposits and commercial, consumer and mortgage loans. Mortgage banking activities are carried out by the Bank's mortgage banking division, whose principal activity is to originate mortgage loans for the Company's own portfolio. As part of its mortgage banking activities, the Company may sell loans directly into the secondary market or securitize conforming loans into mortgage-backed securities.

Financial Services is comprised of the Bank's trust division, Oriental Financial Services, OFS Securities, Oriental Insurance, and CPC. The core operations of this segment are financial planning, money management and investment banking, brokerage services, insurance sales activity, corporate and individual trust and retirement services, as well as pension plan administration services.

The Treasury segment encompasses all of the Company's asset/liability management activities, such as purchases and sales of investment securities, interest rate risk management, derivatives, and borrowings. Intersegment sales and transfers, if any, are accounted for as if the sales or transfers were to third parties, that is, at current market prices.

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

Following are the results of operations and the selected financial information by operating segment as of and for the quarters and the six-month periods ended June 30, 2013 and 2012:

	Quarter Ended June 30, 2013					
	Banking	Financial Services	Treasury	Total Major Segments	Eliminations	Consolidated Total
			(In thousands)			
Interest income	$ 115,047	$ 96	$ 10,665	$ 125,808	$ -	$ **125,808**
Interest expense	(10,272)	-	(10,167)	(20,439)	-	**(20,439)**
Net interest income	104,775	96	498	105,369	**-**	**105,369**
Provision for non-covered loan and lease losses	(37,527)	-	-	(37,527)	-	**(37,527)**
Provision for covered loan and lease losses	(1,211)	-	-	(1,211)	-	**(1,211)**
Non-interest income (loss)	(4,197)	8,100	3,893	7,796	-	**7,796**
Non-interest expenses	(57,918)	(6,650)	(4,254)	(68,822)	-	**(68,822)**
Intersegment revenue	579	-	-	579	(579)	-
Intersegment expenses	-	(485)	(94)	(579)	579	-
Income before income taxes	**$ 4,501**	**$ 1,061**	**$ 43**	**$ 5,605**	**$ -**	**$ 5,605**
Total assets	**$ 6,746,902**	**$ 39,960**	**$ 2,527,039**	**$ 9,313,901**	**$ (877,967)**	**$ 8,435,934**

	Quarter Ended June 30, 2012					
	Banking	Financial Services	Treasury	Total Major Segments	Eliminations	Consolidated Total
			(In thousands)			
Interest income	$ 37,565	$ -	$ 23,223	$ 60,788	$ -	$ **60,788**
Interest expense	(5,685)	-	(21,947)	(27,632)	-	**(27,632)**

Net interest income	31,880	-	1,276	33,156	**-**	**33,156**
Provision for non-covered loan and lease losses	(3,800)	-	-	(3,800)	-	**(3,800)**
Provision for covered loan and lease losses, net	(1,467)	-	-	(1,467)	-	**(1,467)**
Non-interest income	33	5,941	11,862	17,836	-	**17,836**
Non-interest expenses	(24,365)	(3,611)	(1,734)	(29,710)	-	**(29,710)**
Intersegment revenue	440	-	-	440	(440)	-
Intersegment expenses	-	(296)	(144)	(440)	440	-
Income before income taxes	**$ 2,721**	**$ 2,034**	**$ 11,260**	**$ 16,015**	**$ -**	**$ 16,015**
Total assets	**$ 3,116,655**	**$ 15,143**	**$ 3,951,720**	**$ 7,083,518**	**$ (707,240)**	**$ 6,376,278**

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

	Six-Month Period Ended June 30, 2013					
	Banking	Financial Services	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 216,571	$ 182	$ 22,683	$ 239,436	$ -	$ **239,436**
Interest expense	(21,417)	-	(20,068)	(41,485)	-	**(41,485)**
Net interest income	195,154	182	2,615	197,951	**-**	**197,951**
Provision for non-covered loan and lease losses	(45,443)	-	-	(45,443)	-	**(45,443)**
Provision for covered loan and lease losses, net	(1,883)	-	-	(1,883)	-	**(1,883)**
Non-interest income (loss)	(901)	15,801	4,030	18,930	-	**18,930**
Non-interest expenses	(115,834)	(12,777)	(7,020)	(135,631)	-	**(135,631)**
Intersegment revenue	(624)	-	-	(624)	624	-
Intersegment expenses	-	(786)	1,410	624	(624)	-
Income before income taxes	**$ 30,469**	**$ 2,420**	**$ 1,035**	**$ 33,924**	**$ -**	**$** 33,924

	Six-Month Period Ended June 30, 2012					
	Banking	Financial Services	Treasury	Total Major Segments	Eliminations	Consolidated Total
	(In thousands)					
Interest income	$ 77,229	$ -	$ 53,479	$ 130,708	$ -	$ **130,708**
Interest expense	(12,094)	-	(46,472)	(58,566)	-	**(58,566)**
Net interest income	65,135	-	7,007	72,142	**-**	**72,142**
Provision for non-covered loan and lease losses	(6,800)	-	-	(6,800)	-	**(6,800)**
Provision for covered loan and lease losses, net	(8,624)	-	-	(8,624)	-	**(8,624)**
Non-interest income	701	11,731	18,563	30,995	-	**30,995**
Non-interest expenses	(46,952)	(8,500)	(3,657)	(59,109)	-	**(59,109)**
Intersegment revenue	844	-	-	844	(844)	-

Intersegment expenses	-	(605)	(239)	(844)	844	-
Income before income taxes	**$ 4,304**	**$ 2,626**	**$ 21,674**	**$ 28,604**	**$ -**	**$ 28,604**

NOTE 19 – SUBSEQUENT EVENTS

On August 1, 2013, upon receipt of the required approval of the Financial Industry Authority, OFS Securities merged with and into Oriental Financial Services.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INTRODUCTION

The following discussion of the Company's financial condition and results of operations should be read in conjunction with the "Selected Financial Data" and the Company's unaudited consolidated financial statements and related notes. This discussion and analysis contains forward-looking statements. Please see "Forward-Looking Statements" and the risk factors set forth in our 2012 Form 10-K for discussion of the uncertainties, risks and assumptions associated with these statements.

The Company is a publicly-owned financial holding company that provides a full range of banking and financial services through its subsidiaries, including commercial, consumer , auto and mortgage lending; checking and savings accounts; financial planning, insurance and securities brokerage services; and corporate and individual trust and retirement services. The Company operates through three major business segments: Banking, Financial Services, and Treasury, and distinguishes itself based on quality service. The Company has 56 branches in Puerto Rico and a subsidiary in Boca Raton, Florida. 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 diversified mix of businesses and products generates both the interest income traditionally associated with a banking institution and non-interest income traditionally associated with a financial services institution (generated by such businesses as securities brokerage, fiduciary services, investment banking, insurance agency, and retirement plan administration). Although all of these businesses, to varying degrees, are affected by interest rate and financial market fluctuations and other external factors, the Company's commitment is to continue producing a balanced and growing revenue stream.

The BBVAPR Acquisition, the deleveraging of the Company's investment securities portfolio, and the continued organic growth of its banking operations have transformed the profitability of the Company in line with its strategic direction. The Company has begun to realize the anticipated benefits of the BBVAPR Acquisition as reflected by its significantly larger and higher yielding loan assets, a significantly larger deposit base and balances, and a sharply reduced size of its investment securities portfolio. It expects to continue to benefit from a more diverse business portfolio as well as increased scale and leadership in its market.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with U.S. Generally Accepted Accounting Principles ("GAAP") requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expenses in the consolidated financial statements. Understanding our accounting policies and the extent to which we use management judgment and estimates in applying these policies is integral to understanding our financial statements. We provide a summary of our significant accounting policies in "Note 1—Summary of Significant Accounting Policies" of our annual report on 2012 Form 10-K for the year ended December 31, 2012 (the "2012 Form 10-K").

In the "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates" section of our 2012 Form 10-K, we identified the following accounting policies as critical because they require significant judgments and assumptions about highly complex and inherently uncertain matters and the use of reasonably different estimates and assumptions could have a material impact on our reported results of operations or financial condition:

- Business combination
- Allowance for loan and lease losses
- Financial instruments

We evaluate our critical accounting estimates and judgments on an ongoing basis and update them as necessary based on changing conditions. Management has reviewed and approved these critical accounting policies and has discussed its judgments and assumptions with the Audit and Compliance Committee of our Board of Directors. There have been no material changes in the methods used to formulate these critical accounting estimates from those discussed in our 2012 Form 10-K.

OVERVIEW OF FINANCIAL PERFORMANCE

SELECTED FINANCIAL DATA

	Quarter Ended June 30,			Six-Month Period Ended June 30,		
	2013	2012	Variance %	2013	2012	Variance %
EARNINGS DATA:	(In thousands, except per share data)					
Interest income	$ 125,808	$ 60,788	107.0%	$ 239,436	$ 130,708	83.2%
Interest expense	20,439	27,632	-26.0%	41,485	58,566	-29.2%
Net interest income	**105,369**	**33,156**	**217.8%**	**197,951**	**72,142**	**174.4%**
Provision for non-covered loan and lease losses	37,527	3,800	887.6%	45,443	6,800	568.3%
Provision for covered loan and lease losses, net	1,211	1,467	-17.5%	1,883	8,624	-78.2%
Total provision for loan and lease losses, net	**38,738**	**5,267**	**635.5%**	**47,326**	**15,424**	**206.8%**
Net interest income after provision for loan and lease losses	**66,631**	**27,889**	**138.9%**	**150,625**	**56,718**	**165.6%**
Non-interest income	7,796	17,836	-56.3%	18,930	30,995	-38.9%
Non-interest expenses	68,822	29,710	131.6%	135,632	59,109	129.5%
Income before taxes	**5,605**	**16,015**	**-65.0%**	**33,923**	**28,604**	**18.6%**
Income tax expense (benefit)	(31,934)	1,057	-3121.2%	(24,808)	2,994	-928.6%
Net income	**37,539**	**14,958**	**151.0%**	**58,731**	**25,610**	**129.3%**
Less: dividends on preferred stock	(3,466)	(1,201)	153.0%	(6,931)	(2,401)	**-188.7%**
Income available to common	**$ 34,073**	**$ 13,757**	**147.7%**	**$ 51,800**	**$ 23,209**	**123.2%**

shareholders									
PER SHARE DATA:									
Basic	**$**	**0.75**	**$**	**0.34**	**120.9%**	**$**	**1.14**	**$**	**0.57**	**100.0%**
Diluted	**$**	**0.68**	**$**	**0.34**	**101.1%**	**$**	**1.05**	**$**	**0.57**	**84.8%**
Average common shares outstanding		**45,630**		**40,703**	**12.1%**		**45,613**		**40,873**	**11.6%**
Average common shares outstanding and equivalents		**52,968**		**40,808**	**29.8%**		**52,929**		**40,986**	**29.1%**
Cash dividends declared per common share	**$**	**0.06**	**$**	**0.06**	**20.0%**	**$**	**0.12**	**$**	**0.12**	**0.0%**
Cash dividends declared on common shares	**$**	**2,742**	**$**	**2,444**	**12.2%**	**$**	**5,479**	**$**	**4,887**	**12.1%**
PERFORMANCE RATIOS:										
Return on average assets (ROA)		**1.77%**		**0.91%**	**94.5%**		**1.36%**		**0.79%**	**72.2%**
Return on average common equity (ROE)		**18.56%**		**8.69%**	**113.6%**		**14.29%**		**7.38%**	**93.6%**
Equity-to-assets ratio		**10.34%**		**10.86%**	**-4.8%**		**10.34%**		**10.86%**	**-4.8%**
Efficiency ratio		**53.24%**		**66.55%**	**-20.0%**		**55.35%**		**62.16%**	**-10.9%**
Interest rate spread		**5.55%**		**2.24%**	**147.8%**		**5.11%**		**2.38%**	**114.7%**
Interest rate margin		**5.56%**		**2.29%**	**142.8%**		**5.13%**		**2.45%**	**109.4%**

SELECTED FINANCIAL DATA - (Continued)

PERIOD END BALANCES AND CAPITAL RATIOS:		June 30, 2013		December 31, 2012	Variance %
		(In thousands, except per share data)			
Investments and loans					
Investments securities	$	1,860,660	$	2,233,265	-16.7%
Loans and leases not covered under shared-loss agreements with the FDIC, net		4,621,649		4,773,923	-3.2%
Loans and leases covered under shared-loss agreements with the FDIC, net		369,380		395,307	-6.6%
Securities sold but not yet delivered		16,732		-	100.0%
Total investments and loans	**$**	**6,868,421**	**$**	**7,402,495**	**-7.2%**
Deposits and borrowings					
Deposits	$	5,665,038	$	5,689,559	-0.4%
Securities sold under agreements to repurchase		1,313,870		1,695,247	-22.5%
Other borrowings		421,261		792,425	-46.8%
Total deposits and borrowings	**$**	**7,400,169**	**$**	**8,177,231**	**-9.5%**
Stockholders' equity					
Preferred stock	$	176,000	$	176,000	0.0%
Common stock		52,689		52,671	0.0%
Additional paid-in capital		538,105		537,453	0.1%
Legal surplus		57,906		52,143	11.1%
Retained earnings		111,292		70,734	57.3%
Treasury stock, at cost		(80,834)		(81,275)	0.5%
Accumulated other comprehensive income		15,766		55,880	-71.8%
Total stockholders' equity	**$**	**870,924**	**$**	**863,606**	**0.8%**
Per share data					
Book value per common share	**$**	**15.45**	**$**	**15.31**	**0.9%**
Tangible book value per common share	**$**	**13.49**	**$**	**13.31**	**1.4%**
Market price at end of period	**$**	**18.11**	**$**	**13.35**	**35.7%**
Capital ratios					
Leverage capital		**8.54%**		**6.42%**	**33.0%**
Tier 1 risk-based capital		**13.96%**		**12.94%**	**7.9%**
Total risk-based capital		**16.02%**		**15.15%**	**5.7%**
Tier 1 common equity to risk-weighted assets		**9.97%**		**9.11%**	**9.5%**
Financial assets managed					
Trust assets managed	$	2,638,787	$	2,514,401	4.9%
Broker-dealer assets gathered	$	2,822,395		2,722,196	3.7%

Financial Highlights

Income available to common shareholders for the quarter and six-month period ended June 30, 2013, increased to $34.1 million and $51.8 million, or $0.68 and $1.05 per diluted share, respectively. The income available to common shareholders are a significant improvement over the $13.8 million and $23.2 million for the quarter and six-month period ended June 30, 2012, respectively.

Interest income from loans for the quarter and six-month period ended June 30, 2013, increased 205.1% and 178.5% when compared with the same periods in 2012, while net interest margin expanded to 5.56% from 2.29% in the second quarter of 2012, and to 5.13% for the six-month period ended June 30, 2013, from 2.45% for the same period in 2012.

During the quarter ended June 30, 2013, the Company's return on assets was 1.77%, and its return on equity was 18.56%, all of which represent improvements from the second quarter of 2012. The Company improved its efficiency ratio, which decreased to 53.24% from 66.55% when compared with the same quarter in 2012. For the six-month period ended June 30, 2013, the Company's return on assets was 1.36% and its return on equity was 14.29%, both of which also represent improvements from the same period in 2012. The efficiency ratio decreased to 55.35% from 62.16% when compared with the same period in 2012.

Operating revenues for the quarter ended June 30, 2013 increased 121.9%, or $62.2 million, to $113.2 million when compared to the same period in 2012. Operating revenues for the six-month period ended June 30, 2013 increased 110.3%, or $113.7 million, to $216.9 million when compared to the same period in 2012.

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
OPERATING REVENUE				
Net interest income	$ 105,368	$ 33,156	$ 197,951	$ 72,141
Non-interest income, net	7,796	17,836	18,930	30,995
Total operating revenue	**$ 113,164**	**$ 50,992**	**$ 216,881**	**$ 103,136**

Interest Income

Total interest income for the quarter and six-month period ended June 30, 2013 increased 107.0% to $125.8 million and 83.2% to $239.4 million, respectively, as compared to the same periods in 2012. This was a result of an increase in interest income from loans of $77.0 million, or 205.1%, and $137.8 million, or 178.5%, when compared to the quarter and six-month period ended June 30, 2012, respectively. This increase was partially offset by a decrease in interest income from investments of $12.0 million, or 51.8%, and $29.1 million, or 54.5%, compared to the quarter and six-month period ended June 30, 2012, respectively. This result was related to the BBVAPR Acquisition in which the non-covered loans portfolio increased by approximately $3.4 billion when compared to same period in 2012. In addition, the yield on covered loans increased from 17.75% and 17.64% for the quarter and six-month period ended June 30, 2012, respectively, to 25.62% and 23.10% for the quarter and six-month period ended June 30, 2013. This increase in yield is the result of higher projected cash flows on certain pools of covered loans, as credit losses have been lower than initially estimated for these loan pools. The covered portfolio is beginning to have cost recoveries on pools with lower carrying amounts, and these have the effect of increasing net interest income. Such cost recoveries for the quarter ended June 30, 2013 amounted to $6.2 million in the leasing and the construction loan pools. The accretable yield amounted to $167.1 million at June 30, 2013 compared to $188.0 million at December 31, 2012.

Interest income from investments reflects a 51.8% and 54.5% decrease for the quarter and six-month period ended June 30, 2013, as compared to the same period in 2012, primarily related to the lower balance in the investment securities portfolio due to the sale of investments securities as part of the deleverage executed during the third and fourth quarters of 2012 in connection with the BBVAPR Acquisition

Interest Expense

Total interest expense for the quarter and six-month period ended June 30, 2013 decreased 26.0% to $20.4 million and 29.2% to $41.5 million, respectively, as compared to the same periods in 2012. This reflects the lower cost of both securities sold under agreements to repurchase (2.10% vs. 2.16%; 1.99% vs. 2.23%) and deposits (0.71% vs. 1.40%; 0.73% vs. 1.48%) for the quarter and six-month period ended June 30, 2013, respectively, as compared to the same periods in 2012, which reflects continuing progress in the repricing of the Group's core retail deposits and further reductions in its cost of funds, in addition to the reduction in the repurchase agreements as a result of the deleverage executed during the third and fourth quarters of 2012 in connection with the BBVAPR Acquisition.

Net Interest Income

Net interest income for the quarter and six-month period ended June 30, 2013 was $105.4 million and $198.0 million, respectively, an increase of 217.8% and 174.4%, respectively, when compared with the same periods in 2012. The increase was mostly due to the net effect of an increase of 426.1% and 383.4% for the quarter and six-month period ended June 30, 2013, respectively, in interest income from non-covered loans as a result of higher loan balances following the BBVAPR Acquisition. It is also due to a decrease of 26.0% and 29.2% in interest expense for the same respective periods due to lower cost of funds, partially offset by a decrease of 51.8% and 54.5% for the same respective periods on interest income from investments, related to lower balances from aforementioned deleverage transactions and a lower yield in the investment securities portfolio.

Net interest margin of 5.56% and 5.13% for the quarter and six-month period ended June 30,2013, respectively, increased 327 basis points and 268 basis points when compared to the quarter and six-month period ended June 30, 2012.

Provision for Loan and Lease Losses

Provision for non-covered loans losses for the quarter and six-month period ended June 30, 2013 increased $33.7 million and $38.6 million, respectively, when compared to the same periods in 2012. The increased is mostly due to the net impact of $21.0 million in additional provision for loan and lease losses due to reclassification to held-for-sale of non-performing residential mortgage loans with unpaid principal balance of $59 million and the increase in loan averages balances in 2013. Provision for covered loans losses for the quarter and six-month period ended June 30, 2013 decreased $56 thousand and $6.7 million when compared to the same periods ended June 30, 2012, as some covered construction and development and commercial real estate loan pools underperformed during the second quarter of 2012, which required a provision amounting to $7.2 million, net of the estimated reimbursement from the FDIC , compared to the recorded net provision of $1.2 million resulting from this quarter's assessment of actual versus expected cash flows on the covered portfolio accounted for under the provisions of ASC 310-30.

Non-Interest Income

During the quarter and six-month period ended June 30, 2013, core banking and financial services revenues increased 108.0% to $23.9 million and 105.1% to $47.1 million, respectively, as compared to the same periods in 2012, primarily reflecting a $10.2 million and $19.5 million increase in banking services revenue to $13.3 million and $25.7 million for the quarter and six-month period ended June 30, 2013, respectively, attributed to an increase of 157.6% in deposits from June 30, 2012, which is principally attributed to the BBVAPR Acquisition.

Net FDIC shared-loss expense of $20.0 million and $32.8 million for the quarter and six-month period ended June 30, 2013, respectively, compared to $5.6 million and $10.4 million for the same periods in 2012. Such increase resulted from the ongoing evaluation of expected cash flows of the loan portfolio acquired in the FDIC-assisted acquisition. As a result of such evaluation, the Company expects a decrease in losses to be collected from the FDIC and the improved re-yielding of the accretable yield on the covered loans. This reduction in claimable losses amortizes the shared-loss indemnification asset through the life of the shared-loss agreements. This amortization is net of the accretion of the discount recorded to reflect the expected claimable loss at its net present value. During the quarter ended June 30, 2013 the net amortization included $7.1 million of additional amortization of the FDIC indemnification asset from stepped up cost recoveries on certain construction and leasing loan pools.

There was no gain or loss on the sale of securities in the quarter and six-month period ended June 30, 2013 as compared to gains of $12.0 million and $19.3 million in the same periods in 2012.

Non-Interest Expense

Non-interest expense increased to $68.8 million and $135.6 million for the quarter and six-month period ended June 30, 2013, respectively, compared to $29.7 million and $59.1 million in the same periods of the previous year, due to the Company's expanded operations as a result of the BBVAPR Acquisition, including merger and restructuring costs of $5.3 million and $10.8 million for the quarter and six-month period, respectively. Also, the quarter and six-month period ended June 30, 2013 reflects a $2.0 million impact of the new 1.0% tax on gross revenues, recently enacted in the amendments to the Puerto Rico tax code.

The efficiency ratio for the quarter and six-month period ended June 30, 2013 was 53.24% and 55.35%, respectively, compared to 66.55% and 62.16% for the quarter and six-month period ended June 30, 2012, respectively.

Income Tax Expense

Income tax benefit was $31.9 million and $24.8 million for the quarter and six-month period ended June 30, 2013, respectively, compared to an expense of $1.1 million and $3.0 million for the same periods in 2012. The income tax benefit of $31.9 million for the quarter ended June 30, 2013 includes three items resulting from the recent amendment to the Puerto Rico tax code: (i) a $37.0 million benefit from an increase in the Company's deferred tax asset as a result of the increase in corporate income taxes to 39% from 30%; (ii) the Company's income tax expense at the Company's higher effective rate of 35.5% for the second quarter of 2013; and (iii) the increase in the Company's income tax expense for the first quarter of 2013 as a result of the increase in the effective tax rate to 35.5% from the previously reported 25.2%.

Income Available to Common Shareholders

For the quarter and six-month period ended June 30, 2013, the Group's income available to common shareholders amounted to $34.1 million and $51.8 million, respectively, compared to $13.8 million and $23.2 million for the same periods in 2012. Earnings per basic common share and fully diluted common share were $0.75 and $0.68 for the quarter ended June 30, 2013, respectively, compared to earnings per basic and fully diluted common share of $0.34 for the quarter ended June 30, 2012. Income per basic common share and fully diluted common share were $1.14 and $1.04, respectively, for the six-month period ended June 30, 2013, compared to income per basic and fully diluted common share of $0.57 for the six-month period ended June 30, 2012.

Interest Earning Assets

The loan portfolio declined to $4.991 billion at June 30, 2013 compared to $5.169 billion at December 31, 2012 primarily due to the early pay down of some commercial loans and the reclassification of non-performing residential mortgage loans with a book value of $55 million to held-for-sale, at fair value. The investment portfolio of $1.861 billion at June 30, 2013 decreased 9.2% compared to $2.233 billion at December 31, 2012. The decrease in the investment portfolio is mainly due to redemptions and maturities of investments securities available for sale.

Interest Bearing Liabilities

Total deposits decreased slightly to $5.665 billion at June 30, 2013, compared to $5.690 billion at December 31, 2012. Core deposits, including brokered deposits, increased 2.7% compared to December 31, 2012, while brokered certificate of deposits decreased 16.6%. Securities sold under agreements to repurchase decreased 22.5%, or $381.4 million, as the Company used available cash to pay off $380 million repurchase agreements at maturity. During the six-month period ended June 30, 2013, the Company settled, prior to maturity, a former BBVAPR subordinated note of $50 million.

Stockholders' Equity

Stockholders' equity at June 30, 2013 was $870.9 million compared to $863.6 million at December 31, 2012, an increase of 0.8%. This increase reflects the net income for the quarter, partially offset by the change in other comprehensive income.

Book value per share was $15.45 at June 30, 2013 compared to $15.31 at December 31, 2012.

The Company maintains capital ratios in excess of regulatory requirements. At June 30, 2013, Tier 1 Leverage Capital Ratio was 8.54%, Tier 1 Risk-Based Capital Ratio was 13.96%, and Total Risk-Based Capital Ratio was 16.02%.

Return on Average Assets and Common Equity

Return on average common equity (“ROE”) for the quarter and six-month period ended June 30, 2013 was 18.56% and 14.29%, respectively, up from 8.69% and 7.38% for the quarter and six-month period ended June 30, 2012, respectively. Return on average assets (“ROA”) for the quarter and six-month period ended June 30, 2013 was 1.77% and 1.36%, respectively, up from 0.91% and 0.79% for the same periods in 2012. The increases in ROE and ROA is mostly due to a 151.0% and 129.3% increase in net income from $15.0 million and $25.6 million in the quarter and six-month period ended June 30, 2012, respectively, to $37.5 million and $58.7 million in the quarter and six-month period ended June 30, 2013, respectively.

Assets under Management

Assets managed by the Company’s trust division, the retirement plan administration subsidiary (CPC), and the broker-dealer subsidiaries increased from December 31, 2012. The trust division offers various types of individual retirement accounts (“IRA”) and manages 401(k) and Keogh retirement plans and custodian and corporate trust accounts, while CPC manages the administration of private retirement plans. At June 30, 2013, total assets managed by the Company’s trust division and CPC increased 1.7% to $2.639 billion, compared to $2.514 billion at December 31, 2012, mainly related to employer and employee account contributions and capital market appreciation. At June 30, 2013, total assets managed by the broker-dealer subsidiaries from its customer investment accounts increased 1.1% to $2.822 billion, compared to $2.722 billion at December 31, 2012.

Lending

Total loan production of $601.7 million for the six-month period ended June 30, 2013 increased 190.8% year over year, including $327.0 million in the quarter ended June 30, 2013. Total commercial loan production of $178.3 million for the six-month period ended June 30, 2013, increased 95.5% from the same period in 2012, including $104.3 million in the quarter ended June 30, 2013. These increases are directly related to the BBVAPR Acquisition as the Company continue building a strong institutional pipeline.

Mortgage loan production and purchases of $101.3 million and $178.4 million for the quarter and six-month period ended June 30, 2013, respectively, increased 107.1% and 89.9% from the same periods in 2012. The Company sells most of its conforming mortgages in the secondary market and retains the servicing rights. The increase in mortgage loan production is also the result of the benefits of the completion during this quarter, of the integration of the BBVPR and Oriental mortgage operations.

Consumer loans production for the quarter and six-month period ended June 30, 2013 totaled $26.6 million and $49.2, up 247.0% and 283.3% when compared with the same periods in 2012. The increase in consumer lending is the result of the benefits of a larger branch network and origination platform following the BBVAPR Acquisition.

Auto and leasing production for the quarter and six-month period ended June 30, 2013 totaled $94.7 million and $195.7 million, respectively, up from $4.4 million and $8.9 million in the quarter and six-month period ended June 30, 2012, respectively. The increase is mainly attributed to the auto loan business newly entered into by the Company following the BBVAPR Acquisition.

While the loan portfolio remains far greater than it was a year ago and loan production for the quarter and six-month period ended June 30, 2013 has increased considerably from the same periods in 2012, total loan portfolio have declined slightly by $178.2 million from $5.169 billion at December 31, 2012 to $4.991 billion at June 30, 2013, mostly as the result of scheduled pay downs and maturities in both the non-covered and covered portfolios, a scheduled pay down of a PR government obligation of about $125 million, and the reclassification of residential non-performing loans to held-for-sale.

Credit Quality on Non-Covered Loans

Net credit losses, excluding acquired loans, increased $28.8 million to $32.6 million, and $29.5 million to $35.9 million during the quarter and six-month period ended June 30, 2013, respectively, representing 8.86% and 5.11% of average non-covered loans outstanding, versus 1.25% and 1.07% in the same periods in 2012. The credit losses for the quarter and six-month periods ended June 30, 2013 include a $27 million charge-off from nonperforming mortgage loans transferred into the loan held-for-sale category. The allowance for loan and lease losses on non-covered loans increased to $46.6 million (2.62% of total non-covered loans) at June 30, 2013, compared to $39.9 million (3.21% of total non-covered loans) at December 31, 2012.

Non-performing loans ("NPLs"), which exclude loans covered under shared-loss agreements with the FDIC and loans acquired in the BBVAPR Acquisition accounted under ASC 310-30, decreased to $88.5 million at June 30, 2013 compared to $145.1 million at December 31, 2012 primarily due to the reclassification of certain non-performing residential mortgage loans with a net book value of $55.0 million, to the loan held-for-sale category. Without this re-class to loans held-for-sale, NPL balances would have been relatively consistent between December 31, 2012 and June 31, 2013.

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 on 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 quarter and six-month period ended June 30, 2013, the Company's pre-tax pre-provision operating income was approximately $65.7 million and $120.2 million, respectively, an increase of 340.1% and 234.0% from $14.9 million and $36.0 million in the same periods of last year. Pre-tax pre-provision operating income is calculated as follows:

	Quarter Ended June 30,		Six-Month Period Ended June 30,	
	2013	2012	2013	2012
	(In thousands)		(In thousands)	
PRE-TAX PRE-PROVISION OPERATING INCOME				
Net interest income	$ 105,369	$ 33,156	$ 197,951	$ 72,142
Core non-interest income:				
Financial service revenue	8,030	5,903	15,690	11,791

Banking service revenue		13,334		3,145		25,716		6,225
Mortgage banking activities		2,525		2,436		5,679		4,938
Total core non-interest income		**23,889**		**11,484**		**47,085**		**22,954**
Non-interest expenses		(68,822)		(29,710)		(135,632)		(59,109)
Less merger and restructuring charges		5,274		-		10,808		-
		(63,548)		(29,710)		(124,824)		(59,109)
Total pre-tax pre-provision operating income	**$**	**65,710**	**$**	**14,930**	**$**	**120,212**	**$**	**35,987**

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Tangible common equity consists of common equity less goodwill and core deposit intangibles. Tier 1 common equity consists of common equity less goodwill, core deposit intangibles, net unrealized gains on available for sale securities, net unrealized losses on cash flow hedges, and disallowed deferred tax asset and servicing assets. Ratios of tangible common equity to total assets, tangible common equity to risk-weighted assets, total equity to risk-weighted assets and Tier 1 common equity to risk-weighted assets are non-GAAP measures.

At June 30, 2013, tangible common equity to total assets and tangible common equity to risk-weighted assets increased to 7.30% and 12.22%, respectively, from 6.73% and 11.82% at December 31, 2012. Total equity to risk-weighted assets and Tier 1 common equity to risk-weighted assets at June 30, 2013 increased to 17.30% and 9.97%, respectively, from 16.48% and 9.11% at December 31, 2012

Ratios calculated based upon Tier 1 common equity have become a focus of regulators and investors, and management believes ratios based on Tier 1 common equity assist investors in analyzing the Company's capital position. Furthermore, 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. Neither Tier 1 common equity nor tangible common equity or related measures should be considered in isolation or as a substitute for stockholders' equity, total assets or any other measure calculated in accordance with GAAP.

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 quarters
and six-month periods ended June 30, 2013 and 2012:

TABLE 1 - QUARTERLY ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE
FOR THE QUARTERS ENDED JUNE 30, 2013 AND 2012

	Interest		Average rate		Average balance	
	June 2013	June 2012	June 2013	June 2012	June 2013	June 2012
	(Dollars in thousands)					
A - TAX EQUIVALENT SPREAD						
Interest-earning assets	**$ 125,808**	**$ 60,788**	**6.64%**	**4.20%**	**$ 7,580,468**	**$ 5,794,684**
Tax equivalent adjustment	1,743	13,675	0.09%	0.94%	-	-
Interest-earning assets - tax equivalent	**127,551**	**74,463**	**6.73%**	**5.14%**	**7,580,468**	**5,794,684**
Interest-bearing liabilities	20,439	27,632	1.09%	1.96%	7,481,718	5,626,256
Tax equivalent net interest income / spread	**107,112**	**46,831**	**5.65%**	**3.18%**	**98,750**	**168,428**
Tax equivalent interest rate margin			**5.64%**	**3.23%**		
B - NORMAL SPREAD						
Interest-earning assets:						
Investments:						
Investment securities	10,925	22,842	2.26%	2.61%	1,936,849	3,501,015
Trading securities	30	4	7.62%	0.00%	1,574	-
Money market investments	243	377	0.18%	0.24%	538,920	634,707
	11,198	**23,223**	**1.81%**	**2.25%**	**2,477,343**	**4,135,722**

Total investments						
Loans not covered under shared-loss agreements with the FDIC:						
Originated and Other loans held-for-investment						
Mortgage	10,494	11,803	5.18%	5.74%	809,898	821,807
Commercial	5,083	4,054	5.10%	5.21%	398,456	311,299
Consumer	1,746	795	9.47%	8.03%	73,776	39,623
Auto and Leasing	5,075	570	10.68%	8.17%	190,129	27,908
Total originated non-covered loans	**22,398**	**17,222**	**6.09%**	**5.74%**	**1,472,259**	**1,200,637**
Acquired						
Mortgage	11,138	-	5.46%	-	816,483	-
Commercial	36,446	-	10.45%	-	1,394,769	-
Consumer	5,101	-	12.36%	-	165,053	-
Auto	15,528	-	7.06%	-	879,936	-
Total acquired non-covered loans	**68,213**	**-**	**8.38%**	**-**	**3,256,241**	**-**
Total non-covered loans	**90,611**	**17,222**	**7.67%**	**5.74%**	**4,728,500**	**1,200,637**
Loans covered under shared-loss agreements with the FDIC:	**23,999**	**20,342**	**25.62%**	**17.75%**	**374,625**	**458,325**
Total loans	**114,610**	**37,564**	**8.98%**	**9.06%**	**5,103,125**	**1,658,962**
Total interest earning assets	**125,808**	**60,787**	**6.64%**	**4.20%**	**7,580,468**	**5,794,684**

	Interest		Average rate		Average balance	
	June 2013	June 2012	June 2013	June 2012	June 2013	June 2012
	(Dollars in thousands)					
Interest-bearing liabilities:						
Deposits:						
Non-interest bearing deposits	-	-	0.00%	0.00%	766,574	172,615
NOW accounts	1,966	2,268	0.57%	1.04%	1,388,689	876,041
Savings and money market accounts	3,014	544	1.35%	0.93%	895,377	234,762
Individual retirement accounts	1,552	2,080	1.71%	2.25%	362,839	369,519
Retail certificates of deposit	2,898	1,667	1.68%	2.02%	690,229	330,644
Total core deposits	**9,430**	**6,559**	**0.92%**	**1.32%**	**4,103,708**	**1,983,581**
Institutional certificates of deposit	2,664	506	1.63%	2.12%	653,270	95,382
Brokered deposits	1,790	851	0.83%	2.04%	858,769	167,207
	4,454	**1,357**	**1.18%**	**2.07%**	**1,512,039**	**262,589**
Deposits fair value premium amortization	(4,326)	(67)	-	-	-	-
Core deposit intangible amortization	415	36	-	-	-	-
Total deposits	**9,973**	**7,885**	**0.71%**	**1.40%**	**5,615,747**	**2,246,170**
Borrowings:						
Securities sold under agreements to repurchase	7,109	16,500	2.10%	2.16%	1,356,856	3,057,598
Advances from FHLB and other borrowings	2,187	2,926	2.14%	4.09%	409,742	286,405
Subordinated capital notes	1,170	321	4.74%	3.56%	98,644	36,083
Total borrowings	**10,466**	**19,747**	**2.24%**	**2.34%**	**1,865,242**	**3,380,086**

Total interest bearing liabilities	**20,439**	**27,632**	**1.09%**	**1.96%**	**7,480,989**	**5,626,256**
Net interest income / spread	**$ 105,369**	**$ 33,156**	**5.55%**	**2.24%**		
Interest rate margin			**5.56%**	**2.29%**		
Excess of average interest-earning assets over average interest-bearing liabilities					**$ 99,479**	**$ 168,428**
Average interest-earning assets to average interest-bearing liabilities ratio					**101.33%**	**102.99%**

C - CHANGES IN NET INTEREST INCOME DUE TO:

	Volume	**Rate**	**Total**
	(In thousands)		
Interest Income:			
Investments	$ (9,312)	$ (2,713)	$ (12,025)
Loans	46,890	30,155	77,045
Total interest income	37,578	27,442	65,020
Interest Expense:			
Deposits	11,831	(9,743)	2,088
Securities sold under agreements to repurchase	(9,178)	(213)	(9,391)
Other borrowings	1,872	(1,762)	110
Total interest expense	4,525	(11,718)	(7,193)
Net Interest Income	**$** 33,053	**$** 39,160	**$** 72,213

TABLE 1/A - YEAR-TO-DATE ANALYSIS OF NET INTEREST INCOME AND CHANGES DUE TO VOLUME/RATE
FOR THE SIX-MONTH PERIOD ENDED JUNE 30, 2013 AND 2012

	Interest		Average rate		Average balance	
	June 2013	June 2012	June 2013	June 2012	June 2013	June 2012
	(Dollars in thousands)					
A - TAX EQUIVALENT SPREAD						
Interest-earning assets	**$ 239,436**	**$ 130,708**	**6.20%**	**4.43%**	**$ 7,721,878**	**$ 5,900,367**
Tax equivalent adjustment	12,336	13,675	0.32%	0.46%	-	-
Interest-earning assets - tax equivalent	**251,772**	**144,383**	**6.52%**	**4.89%**	**7,721,878**	**5,900,367**
Interest-bearing liabilities	41,485	58,566	1.09%	2.05%	7,641,470	5,724,700
Tax equivalent net interest income / spread	**210,287**	**85,817**	**5.43%**	**2.84%**	**80,408**	**175,667**
Tax equivalent interest rate margin			**5.45%**	**2.91%**		
B - NORMAL SPREAD						
Interest-earning assets:						
Investments:						
Investment securities	23,734	52,696	2.35%	2.92%	2,022,072	3,611,510
Trading securities	50	4	8.51%	0.00%	1,175	-
Money market investments	550	779	0.20%	0.25%	544,502	614,517
Total investments	**24,334**	**53,479**	**1.90%**	**2.53%**	**2,567,749**	**4,226,027**
Loans not covered under shared-loss agreements						
with the FDIC:						
Originated						
Mortgage	21,938	24,516	5.41%	5.92%	810,441	828,700
Commercial	9,978	8,150	5.16%	5.34%	386,882	305,116
Consumer	2,942	1,561	9.13%	8.05%	64,412	38,798

Auto and leasing	7,921	1,118	10.97%	8.37%	144,441	26,719
Total originated non-covered loans	**42,779**	**35,345**	**6.08%**	**5.89%**	**1,406,176**	**1,199,333**
Acquired						
Mortgage	22,308	-	5.40%	0.00%	826,101	-
Commercial	62,816	-	8.72%	0.00%	1,441,540	-
Consumer	10,648	-	12.37%	0.00%	172,178	-
Auto	32,323	-	6.99%	0.00%	925,246	-
Total acquired non-covered loans	**128,095**	**-**	**7.61%**	**0.00%**	**3,365,065**	**-**
Total non-covered loans	**170,874**	**35,345**	**7.16%**	**5.89%**	**4,771,241**	**1,199,333**
Loans covered under shared-loss agreements						
with the FDIC:	**44,228**	**41,884**	**23.10%**	**17.64%**	**382,888**	**475,007**
Total loans	**215,102**	**77,229**	**8.35%**	**9.23%**	**5,154,129**	**1,674,340**
Total interest earning assets	**239,436**	**130,708**	**6.20%**	**4.43%**	**7,721,878**	**5,900,367**

	Interest		Average rate		Average balance	
	June 2013	**June 2012**	**June 2013**	**June 2012**	**June 2013**	**June 2012**
		(Dollars in thousands)				
Interest-bearing liabilities:						
Deposits:						
Non-interest bearing deposits	-	-	0.00%	0.00%	766,601	174,497
NOW accounts	5,707	4,817	0.80%	1.11%	1,421,481	869,525
Savings and money market accounts	4,820	1,134	1.10%	0.97%	877,109	235,019
Individual retirement accounts	3,356	4,368	1.83%	2.38%	367,490	367,009
Retail certificates of deposit	6,141	3,795	1.78%	2.20%	691,668	345,644
Total core deposits	20,024	14,114	0.97%	1.42%	4,124,349	1,991,694
Institutional deposits	5,359	1,105	1.71%	2.11%	627,157	104,648
Brokered deposits	3,779	1,893	0.88%	1.84%	857,454	206,049
Total wholesale deposits	9,138	2,998	**1.23%**	1.93%	1,484,611	310,697
Core deposit intangible amortization	829	71	0.00%	0.00%	-	-
Deposits fair value premium amortization	(9,540)	(175)	0.00%	0.00%	-	-
Total deposits	**20,451**	**17,008**	**0.73%**	**1.48%**	**5,608,960**	**2,302,391**
Borrowings:						
Securities sold under agreements to repurchase	14,357	34,070	1.99%	2.23%	1,440,866	3,057,858
Advances from FHLB and other borrowings	3,847	5,930	1.64%	4.17%	469,620	284,188
FDIC-guaranteed term notes	-	909	0.00%	4.11%	-	44,180

Subordinated capital notes	2,830	649	4.65%	3.60%	121,659	36,083
Total borrowings	**21,034**	**41,558**	**2.07%**	**2.43%**	**2,032,145**	**3,422,309**
Total interest bearing liabilities	**41,485**	**58,566**	**1.09%**	**2.05%**	**7,641,105**	**5,724,700**
Net interest income / spread	**$ 197,951**	**$ 72,142**	**5.11%**	**2.38%**		
Interest rate margin			**5.13%**	**2.45%**		
Excess of average interest-earning assets over average interest-bearing liabilities					**$ 80,773**	**$ 175,667**
Average interest-earning assets to average interest-bearing liabilities ratio					**101.06%**	**103.07%**

C - CHANGES IN NET INTEREST INCOME DUE TO:

	Volume	Rate	Total
	(In thousands)		
Interest Income:			
Investments	$ (20,985)	$ (8,160)	$ (29,145)
Loans	97,144	40,729	137,873
Total interest income	**76,159**	**32,569**	**108,728**
Interest Expense:			
Deposits	24,429	(20,986)	3,443
Securities sold under agreements to repurchase	(18,016)	(1,697)	(19,713)
Other borrowings	4,660	(5,471)	(811)
Total interest expense	**11,073**	**(28,154)**	**(17,081)**
Net Interest Income	**$ 65,086**	**$ 60,723**	**$ 125,809**

Net Interest Income

Net interest income amounted to $105.4 million and $198.0 million for the quarter and the six-month period ended June 30, 2013, respectively, a 217.8% and 174.4% increase from $33.2 million and $72.1 million for the same periods in 2012. These changes reflect a decrease of 26.0% and 29.2% in interest expense and an increase of 205.1% and 178.5% in interest income from loans, partially offset by a 51.8% and 54.5% decrease in interest income from investments when comparing the quarter and six-month period ended June 30, 2013 and 2012, respectively.

Interest rate spread for the quarter ended June 30, 2013 increased 331 basis points to 5.55% from 2.24% in the same period of 2012. This increase is mainly due to the net effect of a 87 basis point decrease in the average cost of funds from 1.96% to 1.09%, and a 244 basis point increase in the average yield of interest-earning assets from 4.20% to 6.64%. For the six-month period ended June 30, 2013, interest rate spread increased 273 basis point to 5.11% from 2.38% in the same period of 2012. This increase is mainly due to the net effect of a 96 basis point decrease in the average cost of funds from 2.05% to 1.09%, and a 177 basis point increase in the average yield of interest-earning assets from 4.43% to 6.20%.

The increase in interest income for the quarter was primarily the result of an increase of $37.6 million in interest-earning assets volume variance, and a $27.4 million increase in interest rate variance. The six-month period increase in interest income was primarily the result of an increase of $76.2 million in interest earning assets volume variance, and a $32.6 million increase in interest rate variance. Interest income from loans increased 205.1% to $114.6 million and 178.5% to $215.1 million for the quarter and six-month period ended June 30, 2013, respectively, mainly due to the loan portfolio acquired as part of the BBVAPR Acquisition. This was mitigated by the fact that interest income on investments decreased 51.8% to $11.2 million and 54.5% to $24.3 million in the quarter and six-month period ended June 30, 2013, respectively, compared to the same periods in 2012, reflecting a lower balance in the investment securities portfolio due to the sale of investments securities as part of the deleverage executed during the third and fourth quarters of 2012 in connection with the BBVAPR Acquisition.

Interest expense decreased 26.0% to $20.4 million and 29.2% to $41.5 million for the quarter and six-month period ended June 30, 2013, respectively. The decrease for the quarter was primarily the result of an $11.7 million decrease in interest rate variance, partially offset by a $4.5 million increase in interest-bearing liabilities volume variance. The six-month period decrease was primarily the result of a $28.2 million decrease in interest rate variance, partially offset by an $11.1 million increase in interest-bearing liabilities volume variance. The decrease in interest rate variance is due to a reduction in the cost of funds and the increase in the volume variance is due to the increase in the balance of deposits, which reflected a decrease in cost of funds of 87 basis points to 1.09% and 96 basis points to 1.09% for the quarter and six-month period ended June 30, 2013, respectively, compared to the same periods in 2012. The cost of deposits decreased 69 basis points to 0.71% and 75 basis points to 0.73% for the quarter and six-month period ended June 30, 2013, respectively, compared to 1.40% and 1.48% for the same periods in 2012, primarily due to continuing progress in repricing core deposits and to the maturity of higher cost brokered deposits during the periods. The cost of borrowings decreased by 10 basis points to 2.24% and 36 basis points to 2.07% in the quarter and six-month period ended June 30, 2013, respectively, compared to 2.34% and 2.43% for the same periods in 2012.

For the quarter and six-month period ended June 30, 2013, the average balance of total interest-earning assets was $7.580 billion and $7.722 billion, respectively, an increase of 30.8% for both periods compared to 2012. The increase in average balance of interest-earning assets was mainly attributable to an increase in average loans for the quarter and six-month period ended June 30, 2013 of 207.6% and 207.8% , respectively, resulting from the loan acquisition of the portfolio from BBVAPR, mitigated by a reduction of 40.9% and 39.2% in the average investments for the quarter and the six-month period ended June 30, 2013 as a result of the aforementioned sale of investments as part of the deleverage plan in connection with the BBVAPR Acquisition. For the quarter ended June 30, 2013, the average yield on interest-earning assets was 6.64% compared to 4.20% for the same quarter in 2012, and for the six-month period ended June 30, 2013, was 6.20% compared to 4.43% for the same period in 2012. This was mainly due to the increase in average balance and higher average yields in the non-covered loan portfolio, which their average yield increased to 7.67% from 5.74% and to 7.16% from 5.89% for quarter and six-month period ended June 30, 2013, respectively, compared to the same periods in 2012.

TABLE 2 - NON-INTEREST INCOME SUMMARY

	Quarter Ended June 30,			Six-Month Period Ended June 30,		
	2013	2012	Variance	2013	2012	Variance
	(Dollars in thousands)					
Financial service revenue	$ 8,030	$ 5,903	36.0%	$ 15,690	$ 11,791	33.1%
Banking service revenue	13,334	3,145	324.0%	25,716	6,225	313.1%
Mortgage banking activities	2,525	2,436	3.7%	5,679	4,938	15.0%
Total banking and financial service revenue	**23,889**	**11,484**	**108.0%**	**47,085**	**22,954**	**105.1%**
FDIC shared-loss expense, net	(19,965)	(5,583)	-257.6%	(32,836)	(10,410)	-215.4%
Net gain (loss) on:						
Sale of securities available for sale	-	11,979	-100.0%	-	19,338	-100.0%
Derivatives	1,569	(107)	1566.4%	1,271	(108)	1276.9%
Early extinguishment of subordinated capital notes	-	-	0.0%	1,061	-	100.0%
Other	2,303	63	3555.6%	2,349	(779)	401.5%
	(16,093)	6,352	-353.4%	(28,155)	8,041	-450.1%
Total non-interest income, net	**$ 7,796**	**$ 17,836**	**-56.3%**	**$ 18,930**	**$ 30,995**	**-38.9%**

Non-Interest Income

Non-interest income is affected by the amount of securities, derivatives and trading transactions, the level of trust assets under management, transactions generated by clients’ financial assets serviced by the securities broker-dealer and insurance 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.

As shown in Table 2 above, the Company recorded non-interest income in the amount of $7.8 million and $18.9 million for the quarter and six-month period ended June 30, 2013, respectively, compared to $17.8 million and $31.0 million for the same period in 2012, a decrease of $10.0 million and $12.1 million, respectively.

During the quarter and six-month period ended June 30, 2013, the Company did not have any gain or loss on sale of securities as compared to the quarter and six-month period ended June 30, 2012, in which the Company had gains of $12.0 million and $19.3 million on sale of securities, respectively.

Also, the increase in the FDIC shared-loss expense to $20.0 million and $32.8 million for the quarter and the six-month period ended June 30, 2013, respectively, compared to $5.6 million and $10.4 million for the same periods in 2012, resulted from the ongoing evaluation of expected cash flows of the covered loan portfolio, which resulted in reduced losses expected to be collected from the FDIC and the improved re-yielding of the accretable yield on the covered loans. The reduction in claimable losses amortizes the shared-loss indemnification asset through the life of the shared loss agreement. This amortization is net of the accretion of the discount recorded to reflect the expected claimable loss at its net present value. During the quarter ended June 30, 2013, the Company recorded $7.1 million in additional amortization of the FDIC indemnification asset from stepped up cost recoveries on certain construction and leasing loan pools.

During the quarter ended June 30, 2013, the Company recognized a realized gain of $2.1 million, included as "Net gain (loss) on other" in the Statement of Operations, corresponding to the recovery from the sale of a claim in the Lehman Brothers bankruptcy.

Banking service revenue, which consists primarily of fees generated by deposit accounts, electronic banking services, and customer services, increased 324.0% to $13.3 million and 313.1% to $25.7 million in the quarter and six-month period ended June 30, 2013, respectively, from $3.1 million and $6.2 million for the same periods in 2012. This increase for the quarter and six-month period ended June 30, 2013, is attributable to an increase in transaction volume due to larger the deposit portfolio, as a result of the BBVAPR Acquisition.

Financial service revenue, which consists of commissions and fees from fiduciary activities, and securities brokerage and insurance activities, increased 36.0% to $8.0 million and 33.1% to $15.7 million, for the quarter and six-month period ended June 30, 2013, respectively, compared to $5.9 million and $11.8 million for the same periods in 2012. This increase is mainly due to increased brokerage, trust and insurance business and transactions as a result of the BBVAPR Acquisition.

Income generated from mortgage banking activities increased 3.7% to $2.5 million and 15.0% to $5.7 million for the quarter and six-month period ended June 30, 2013, respectively, compared to $2.4 million and $4.9 million for the same periods in 2012. Such increase is mainly a result of an increase in mortgage loan production for the quarter and six-month period ended June 30, 2013 when compared to the same periods in 2012, as the Company sells the majority of the loans produced into secondary markets. This increase in loan production is partially offset by the effect of the steep rise in interest rate during the later part of the quarter ended June 30, 2013 , resulting in decreased profit margins from the sale of mortgage loans.

TABLE 3 - NON-INTEREST EXPENSES SUMMARY

	Quarter Ended June 30,			Six-Month Period Ended June 30,		
	2013	2012	Variance %	2013	2012	Variance %
	(Dollars in thousands)					
Compensation and employee benefits	$ 24,089	$ 11,184	115.4%	$ 47,338	$ 21,550	119.7%
Occupancy and equipment	8,066	4,292	87.9%	17,282	8,501	103.3%
Professional and service fees	7,710	5,222	47.6%	16,832	10,643	58.2%
Merger and restructuring charges	5,274	-	100.0%	10,808	-	100.0%
Taxes, other than payroll and income taxes	5,132	(107)	4896.3%	7,754	1,067	626.7%
Electronic banking charges	4,094	1,609	154.4%	7,822	3,166	147.1%
Insurance	2,723	1,442	88.8%	5,401	3,262	65.6%
Foreclosure, repossession and other real estate expenses	2,156	936	130.3%	3,661	1,686	117.1%
Loss on sale of foreclosed real estate and other repossessed assets	1,696	886	91.4%	3,573	1,282	178.7%
Loan servicing and clearing expenses	1,884	955	97.3%	3,360	1,923	74.7%
Advertising, business promotion, and strategic	1,670	1,564	6.8%	3,079	2,412	27.7%

initiatives						
Printing, postage, stationery and supplies	851	322	164.3%	2,017	630	220.2%
Communication	835	392	113.0%	1,699	781	117.5%
Director and investor relations	377	342	10.2%	613	651	-5.8%
Other operating expenses	2,265	671	237.6%	4,393	1,555	182.5%
Total non-interest expenses	**$ 68,822**	**$ 29,710**	**131.6%**	**$ 135,632**	**$ 59,109**	**129.5%**
Relevant ratios and data:						
Efficiency ratio	**53.24%**	**66.55%**		**55.35%**	**62.16%**	
Compensation and benefits to non-interest expense	**35.00%**	**37.64%**		**34.90%**	**36.46%**	
Compensation to total assets owned	**1.14%**	**0.70%**		**1.12%**	**0.68%**	
Average number of employees	**1,559**	**751**		**1,573**	**748**	
Average compensation per employee	**$ 61.81**	**$ 59.57**		**$ 60.19**	**$ 57.62**	
Assets owned per average employee	**$ 5,412**	**$ 8,490**		**$ 5,364**	**$ 8,524**	

Non-Interest Expenses

Non-interest expense for the quarter ended June 30, 2013 reached $68.8 million, representing an increase of 131.6% compared to $29.7 million for the quarter ended June 30, 2012. For the six-month period ended June 30, 2013, non-interest expense reached $135.6 million, representing an increase of 129.5% compared to $59.1 million for the same periods in 2012, due to the Company's expanded operations as a result of the BBVAPR Acquisition.

Compensation and employee benefits increased 115.4% and 119.7% to $24.1 million and $47.3 million for the quarter and six-month period ended June 30, 2013, respectively, from $11.2 million and $21.6 million for the same periods in 2012.These increase are mainly driven by the integration of the employees of BBVAPR.

Professional and service fees increased 47.6% to $7.7 million and 58.2% to $16.8 million for the quarter and six-month period ended June 30, 2013, respectively, as compared to $5.2 million and $10.6 million for the same periods in 2012, mainly due to professional expenses related to the BBVAPR integration.

Occupancy and equipment expenses increased 87.9% to $8.1 million and 103.3% to $17.3 million for the quarter and six-month period ended June 30, 2013, as compared to $4.3 million and $8.5 million for the same periods in 2012, as a result of the BBVAPR Acquisition in which the Bank acquired 36 branches and the building where our new headquarters are located. During the quarter ended June 30, 2013, the Company consolidated 8 branches.

Electronic banking charges increased 154.4% to $4.1 million and 147.1% to $7.8 million for the quarter and six-month period ended June 30, 2013, respectively, as compared to $1.6 million and $3.2 million for the same periods in 2012, mostly due to the increase in expenses related to merchant business and card interchange transactions resulting from our banking business growth.

During the quarter and six-month period ended June 30, 2013, the Company incurred $5.3 million and $10.8 million, respectively, in expenses related to the merger and restructuring charges. This amount includes a $3.7 million charge related to an early termination of a contract with a third party servicer of certain loan portfolios acquired in the FDIC-assisted transaction and $3.2 million related to systems integration. These charges represent costs associated with these one-time activities and do not represent ongoing costs of the fully integrated combined organization.

Taxes, other than payroll and income taxes, for the quarter and six-month period ended June 30, 2013 increased to $5.1 million and to $7.8 million, respectively, as compared to a benefit of $107 thousand and an expense of $1.1 million for the same periods in 2012. The increase primarily reflects a $2.0 million impact from the application of the new 1.0% tax on gross revenues which was part of the recently enacted amendments to the Puerto Rico tax code. Also, included in the benefit of $107 thousand during the quarter ended June 30, 2012 was the reversal of an accrual resulting from a municipal license tax settlement.

Foreclosure, repossession and other real estate expenses for the quarter and six-month period ended June 30, 2013 increased 130.3% to $2.2 million and 117.1% to $3.7 million, respectively, as compared to $936 thousand and $1.7 million for the same periods in 2012, principally due to the increase in foreclosures during the six-month period ended June 30, 2013 as compared to the same periods in 2012.

Advertising, business promotion, and strategic initiatives for the quarter and six-month period ended June 30, 2013 increased 6.8% and 27.7%, respectively, as compared to the same periods in 2012, primarily to support the Company's expansion of commercial banking and it's rebranding.

The increase in the Company's net-interest income resulted in a decrease in the efficiency ratio to 53.24% for the quarter ended June 30, 2013 compared to 66.55% for the quarter ended June 30, 2012, and a decrease to 55.35% for the six-month period ended June 30, 2013 from 62.16% from the same period in the prior year. The efficiency ratio measures how much of a company's revenue is used to pay operating expenses. The Company computes its efficiency ratio by dividing non-interest expenses by the sum of its net interest income and non-interest income, but excluding gains on the sale of investments securities, derivatives gains or losses, credit-related other-than-temporary impairment losses, FDIC shared-loss expense, losses on the early extinguishment of repurchase agreements, other gains and losses, and other income that may be considered volatile in nature. Management believes that the exclusion of those items permits greater comparability. Amounts presented as part of non-interest income that are excluded from the efficiency ratio computation amounted to losses of $16.1 million and $28.2 million for the quarter and six-month period ended June 30, 2013, respectively, compared to gains of $6.4 million and $8.0 million for the same period in 2012 . Revenue for purposes of the efficiency ratio for the quarter and six-month period ended June 30, 2013 amounted to $129.3 million and $245.0 million, respectively, compared to $44.6 million and $95.1 million for the same periods in 2012 .

Provision for Loan and Lease Losses

The provision for non-covered loan and lease losses for the quarter and six-month period ended June 30, 2013 totaled $37.5 million and $45.4 million, respectively, an increase of $33.7 million and $38.6 million from the same periods in 2012, mostly due to the net impact of $21.0 million in additional provision for loan and lease losses from the reclassification to held-for-sale of non-performing residential mortgage loans with an unpaid principal balance of $59.0 million. Based on an analysis of the credit quality and the composition of the Company’s loan portfolio, management determined that the provision for the quarter ended June 30, 2013 was adequate in order to maintain the allowance for loan and lease losses at an adequate level to provide for probable losses based upon an evaluation of known and inherent risks.

During the quarter and six-month period ended June 30, 2013, net credit losses amounted to $32.6 million and $35.9 million, respectively, a n increase of 766.0% and 460.8% when compared to $3.8 million and $6.4 million reported for the same periods in 2012. The increase was primarily due to an increase of $27.2 million and a $28.8 million in net credit losses for mortgage loans during the quarter and the six-month period ended June 30, 2013, respectively, compared to the same periods in 2012. These include $27.0 million in charge-offs due to the aforementioned reclassification to held-for-sale of non-performing residential loans with an unpaid principal balance of $59.0 million.

Total charge-offs on originated and other loans held-for-investment increased 757.5% to $33.0 million and 451.3% to $36.5 million for the quarter and six-month period ended June 30, 2013, respectively, as compared to the same periods in 2012, and total recoveries increased from $94 thousand and $216 thousand in the quarter and six-month period ended June 30, 2012, respectively, to $486 thousand and $585 thousand in the quarter and the six-month period ended June 30, 2013, respectively. As a result, the recoveries to charge-offs ratio decreased from 2.44% and 3.26% in the quarter and six-month period ended June 30, 2012 to 1.47% and 1.60% in the quarter and six-month period ended June 30, 2013.

The loans acquired in the BBVAPR Acquisition accounted for under ASC 310-20 (loans with revolving feature and/or acquired at a premium) were recognized at fair value as of December 18, 2012, which included the impact of expected credit losses. Provision for loan and lease losses on these loans for the quarter and the six-month period ended June 30, 2013 was $1.6 million and $3.7 million, respectively. Loans acquired in the BBVAPR Acquisition accounted for under ASC 310-30 (loans acquired with deteriorated credit quality, including those by analogy) were also recognized at fair value as of December 18, 2012, which included the impact of expected credit losses. This portfolio did not require provision for loan and lease losses for the quarter and the six-month period ended June 30, 2013.

The loans covered by the FDIC shared-loss agreement were recognized at fair value as of April 30, 2010, which included the impact of expected credit losses. To the extent credit deterioration occurs in covered loans after the date of acquisition, the Company records an allowance for loan and lease losses. Also, the Company records an increase in the FDIC shared-loss indemnification asset for the expected reimbursement from the FDIC under the shared-loss agreements. Provision for covered loans and lease losses for the quarter and six-month period ended June 30, 2013 was $1.2 million and $1.9 million, reflecting the Company’s quarterly revision of the expected cash flows in the covered loan portfolio considering actual experiences and changes in the Company’s expectations for the remaining terms of the loan pools. During the quarter and six-month period ended June 30, 2012, some covered construction and development and commercial real estate loan pools underperformed, which required a provision amounting to $7.2 million, net of the estimated reimbursement from the FDIC.

Please refer to the “Allowance for Loan and Lease Losses and Non-Performing Assets” section in this MD&A and Table 8 through Table 13 below for more detailed information concerning the allowances for loan and lease losses, net credit losses and credit quality statistics.

Income Taxes

The Company had an income tax benefit of $31.9 million and $24.8 million for the quarter and six-month period ended June 30, 2013, respectively, compared to an expense of $1.1 million and $3.0 million for the same period in 2012. The income tax benefit of $31.9 million for the quarter ended June 30, 2013 includes three items resulting from the recent amendment to the Puerto Rico tax code: (i) a $37.0 million benefit from an increase in the Company’s deferred tax asset as a result of the increase in corporate income taxes to 39% from 30%; (ii) the Company’s income tax expense at the Company’s higher effective rate of 35.4% for the second quarter of 2013; and (iii) the increase in the Company’s income tax expense for the first quarter of 2013 as a result of the increase in the effective tax rate to 35.4% from the previously reported 25.2%.

ANALYSIS OF FINANCIAL CONDITION

TABLE 4 - ASSETS SUMMARY AND COMPOSITION

	June 30, 2013	December 31, 2012	Variance %
	(Dollars in thousands)		
Investments:			
FNMA and FHLMC certificates	$ 1,390,622	$ 1,693,447	-17.9%
Obligations of US Government sponsored agencies	15,113	21,847	-30.8%
US Treasury securities	26,501	26,496	0.0%
CMOs issued by US Government sponsored agencies	248,363	291,400	-14.8%
GNMA certificates	11,180	15,164	-26.3%
Puerto Rico Government and agency obligations	119,695	120,520	-0.7%
FHLB stock	22,156	38,411	-42.3%
Other debt securities	24,755	25,411	-2.6%
Other investments	2,275	568	300.5%
Total investments	**1,860,660**	**2,233,265**	**-16.7%**
Securities sold but not yet delivered	**16,732**	**-**	100.0%
Loans:			
Loans not covered under shared-loss agreements with the FDIC	4,589,924	4,749,300	-3.4%
Allowance for loan and lease losses on non covered loans	(46,625)	(39,921)	-16.8%
Non covered loans receivable, net	**4,543,299**	**4,709,379**	**-3.5%**
Mortgage loans held for sale	78,350	64,544	21.4%
Total loans not covered under shared-loss agreements with the FDIC, net	**4,621,649**	**4,773,923**	**-3.2%**
Loans covered under shared-loss agreements with the FDIC	423,372	449,431	-5.8%
Allowance for loan and lease losses on covered loans	(53,992)	(54,124)	0.2%
Total loans covered under shared-loss agreements with the FDIC, net	**369,380**	**395,307**	-6.6%
Total loans, net	**4,991,029**	**5,169,230**	**-3.4%**
Securities purchased under agreements to resell	**-**	**80,000**	**-100.0%**
Total securities and loans	**6,868,421**	**7,482,495**	**-8.2%**

Other assets:					
Cash and due from banks		737,330		855,490	-13.8%
Money market investments		10,983		13,205	-16.8%
FDIC shared-loss indemnification asset		236,472		286,799	-17.5%
Foreclosed real estate		81,689		73,516	11.1%
Accrued interest receivable		17,508		17,554	-0.3%
Deferred tax asset, net		155,165		122,501	26.7%
Premises and equipment, net		84,301		84,997	-0.8%
Servicing assets		12,994		10,795	20.4%
Derivative assets		19,655		21,889	-10.2%
Goodwill		76,383		76,383	0.0%
Other assets		135,033		150,638	-10.4%
Total other assets		**1,567,513**		**1,713,767**	**-8.5%**
Total assets	**$**	**8,435,934**	**$**	**9,196,262**	**-8.3%**
Investments portfolio composition:					
FNMA and FHLMC certificates		74.9%		75.8%	
Obligations of US Government sponsored agencies		0.8%		1.0%	
US Treasury securities		1.4%		1.2%	
CMOs issued by US Government sponsored agencies		13.3%		13.0%	
GNMA certificates		0.6%		0.7%	
Puerto Rico Government and agency obligations		6.4%		5.4%	
FHLB stock		1.2%		1.7%	
Other debt securities and other investments		1.4%		1.2%	
		100.0%		**100.0%**	

Assets Owned

At June 30, 2013, the Company's total assets amounted to $8.436 billion, a decrease of 8.3% when compared to $9.196 billion at December 31, 2012, and interest-earning assets decreased 8.2% from $7.482 billion at December 31, 2012 to $6.868 billion at June 30, 2013.

At June 30, 2013, loans represented 73% of total interest-earning assets while investments represented 27%, compared to 70% and 30%, respectively, at December 31, 2012.

The Company's loan portfolio is comprised of residential mortgage loans, commercial loans collateralized by mortgages on real estate located in Puerto Rico, other commercial and industrial loans, consumer loans, leases, and auto loans. Auto loans were added as part of the recent BBVAPR Acquisition. At June 30, 2013, the Company's loan portfolio decreased 3.4% to $4.991 billion compared to $5.169 billion at December 31, 2012. The covered loan portfolio decreased $25.9 million, or 6.6%, from December 31, 2012. The non-covered loan portfolio decreased $152.3 million, or 3.2%.

The FDIC shared-loss indemnification asset amounted to $236.5 million as of June 30, 2013 and $286.8 million as of December 31, 2012 ,representing a 17% reduction .The FDIC shared-loss indemnification asset is reduced as claims over losses recognized on covered loans are collected from the FDIC. Realized credit losses in excess of previously forecasted estimates result in an increase in the FDIC shared-loss indemnification asset. Conversely, if realized credit losses are less than previously forecasted estimates, the FDIC shared-loss indemnification asset is amortized through the term of the shared-loss agreements. The decrease in the FDIC shared-loss indemnification asset is mainly related to reimbursements of $18.7 million received from the FDIC during the six-month period ended June 30, 2013, net amortization of $32.8 million and a decrease of $2.1 million in expected net credit impairment losses to be covered under shared-loss agreements, partially offset by $3.2 million in incurred expenses to be reimbursed under the shared-loss agreements.

Investments principally consist of U.S. treasury securities, U.S. government and agency bonds, mortgage-backed securities and Puerto Rico government and agency bonds. At June 30, 2013, the investment portfolio decreased 16.7% to $1.861 billion from $2.233 billion at December 31, 2012. This decrease is mostly due to the effect of a decrease of $302.8 million in FNMA and FHLMC certificates. During the quarter and six-month period ended June 30, 2013, the Company did not have realized gains or losses due to the sale of securities.

TABLE 5 — LOANS RECEIVABLE COMPOSITION

	June 30, 2013	December 31, 2012	Variance %
	(In thousands)		
Loans not covered under shared-loss agreements with FDIC:			
Originated and other loans and leases held for investment:			
Mortgage	$ 755,298	$ 804,942	-6.2%
Commercial	702,074	353,930	98.4%
Auto and leasing	233,092	50,720	359.6%
Consumer	89,608	48,136	86.2%
Total originated and other loans and leases held for investment	**1,780,072**	**1,257,728**	**41.5%**
Acquired loans:			
Accounted for under ASC 310-20			
Commercial and industrial	140,234	317,244	-55.8%
Construction and commercial real estate	14,519	29,215	-50.3%
Auto	373,587	457,894	-18.4%
Consumer	62,751	68,878	-8.9%
	591,091	**873,231**	**-32.3%**
Accounted for under ASC 310-30			
Commercial	747,077	942,267	-20.7%
Construction	140,060	196,692	-28.8%
Mortgage	781,389	810,135	-3.5%
Auto	462,691	554,938	-16.6%
Consumer	88,375	118,171	-25.2%
	2,219,592	**2,622,203**	**-15.4%**
	2,810,683	**3,495,434**	**-19.6%**
	4,590,755	**4,753,162**	**-3.4%**
Deferred loans fees, net	(831)	(3,463)	76.0%
Loans receivable	4,589,924	4,749,699	**-3.4%**
Allowance for loan and lease losses on non-covered loans	(46,625)	(39,921)	-16.8%
Loans receivable, net	**4,543,299**	**4,709,778**	**-3.5%**
Mortgage loans held-for-sale	78,350	64,145	22.1%
Total loans not covered under shared-loss agreements with FDIC, net	**4,621,649**	**4,773,923**	**-3.2%**
Loans covered under shared-loss agreements with FDIC:			
	123,507	128,811	-4.1%

Loans secured by 1-4 family residential properties					
Construction and development secured by 1-4 family residential properties		16,478		15,969	3.2%
Commercial and other construction		275,489		289,070	-4.7%
Leasing		943		7,088	-86.7%
Consumer		6,955		8,493	-18.1%
Total loans covered under shared-loss agreements with FDIC		**423,372**		**449,431**	**-5.8%**
Allowance for loan and lease losses on covered loans		(53,992)		(54,124)	0.2%
Total loans covered under shared-loss agreements with FDIC, net		**369,380**		**395,307**	**-6.6%**
Total loans receivable, net	**$**	**4,991,029**	**$**	**5,169,230**	**-3.4%**

As shown in Table 5 above, total loans receivable net amounted to $5.0 billion at June 30, 2013 compared to $5.2 billion at December 31, 2013.

The Company’s originated and other loans held-for-investment portfolio composition and trends were as follows:

- Mortgage loan portfolio amounted to $755.3 million (42.4% of the gross originated loan portfolio) compared to $804.9 million (64.1% of the gross originated loan portfolio) at December 31, 2012. Mortgage loan production totaled $101.3 million and $178.4 million for the quarter and the six-month period ended June 30, 2013, respectively, increase of 107.2% and 90.0% from $48.9 million and $93.9 million in the previous year quarter and six-month period, respectively.

- Commercial loan portfolio amounted to $702.1 million (39.4% of the gross originated loan portfolio) compared to $353.9 million (28.1% of the gross originated loan portfolio) at December 31, 2012. Commercial loan production increased 193.8% to $104.3 million for the second quarter ended June 30, 2013 and increased 95.5% to $178.3 for the six-month period ended June 30, 2013 from $35.5 million and $91.2 million for the same period in 2012.

- Consumer loan portfolio amounted to $89.6 million (5.0% of the gross originated loan portfolio) compared to $48.1 million (3.8% of the gross originated loan portfolio) at December 31, 2012. Consumer loan production increased 245.5% to $26.6 million for the quarter ended June 30, 2013 and 284.4% to $49.2 million for the six-month period ended June 30, 2013 from $7.7 million and $12.8 million for the same period in 2012.

- Auto and leasing portfolio amounted to $233.1 million (13.0% of the gross originated loan portfolio) compared to $50.7 million (4.0% of the gross originated loan portfolio) at December 31, 2012. Auto and leasing production was $94.7 million for the quarter ended June 30, 2013 and $195.7 million for the six-month period ended June 30, 2013, compared to $4.4 million and $8.9 million for the same period in 2012 in which the Company only originated leases. The auto business line was added as part of the BBVAPR Acquisition on December 18, 2012.

At June 30, 2013 the Company's non-covered BBVAPR acquired loan portfolio composition was as follows :

Portfolio Type		**Carrying Amounts**	**% of Gross Non-Covered Acquired Portfolio**
	(In thousands)		
Mortgage	$	781,389	27.80%

Commercial	1,041,888	37.07%
Consumer	151,124	5.38%
Auto	836,282	29.75%
	$ **2,810,683**	**100.00%**

TABLE 6 - LIABILITIES SUMMARY AND COMPOSITION

	June 30, 2013	December 31, 2012	Variance %
	(Dollars in thousands)		
Deposits:			
Non-interest bearing deposits	$ 872,806	$ 799,667	9.1%
NOW accounts	1,421,563	1,647,072	-13.7%
Savings and money market accounts	909,258	634,133	43.4%
Certificates of deposit	2,457,384	2,603,693	-5.6%
Total deposits	**5,661,011**	**5,684,565**	**-0.4%**
Accrued interest payable	4,027	4,994	-19.4%
Total deposits and accrued interest payable	**5,665,038**	**5,689,559**	**-0.4%**
Borrowings:			
Short term borrowings	-	92,210	-100.0%
Securities sold under agreements to repurchase	1,313,870	1,695,247	-22.5%
Advances from FHLB	285,135	536,542	-46.9%
Federal funds purchased	29,431	9,901	197.3%
Other term notes	7,734	7,734	0.0%
Subordinated capital notes	98,961	146,038	-32.2%
Total borrowings	**1,735,131**	**2,487,672**	**-30.3%**
Total deposits and borrowings	**7,400,169**	**8,177,231**	**-9.5%**
Derivative liabilities	16,701	26,260	-36.4%
Acceptances outstanding	30,571	26,996	13.2%
Other liabilities	117,569	102,169	15.1%
Total liabilities	**$ 7,565,010**	**$ 8,332,656**	**-9.2%**
Deposits portfolio composition percentages:			
Non-interest bearing deposits	15.4%	14.1%	
NOW accounts	25.1%	29.0%	
Savings and money market accounts	16.1%	11.2%	
Certificates of deposit	43.4%	45.7%	
	100.0%	**100.0%**	
Borrowings portfolio composition percentages:			
Short term borrowings	0.0%	3.7%	
Securities sold under agreements to repurchase	75.8%	68.1%	
Advances from FHLB	16.4%	21.6%	
Federal funds purchased	1.7%	0.4%	

Other term notes		0.4%		0.3%
Subordinated capital notes		5.7%		5.9%
		100.0%		**100.0%**
Securities sold under agreements to repurchase				
Amount outstanding at period-end	$	1,313,870	$	1,695,247
Daily average outstanding balance	$	1,440,866	$	2,888,558
Maximum outstanding balance at any month-end	$	1,695,247	$	3,060,578

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Liabilities and Funding Sources

As shown in Table 6 above, at June 30, 2013, the Company's total liabilities were $7.565 billion, 9.2% less than the $8.333 billion reported at December 31, 2012. Deposits and borrowings, the Company's funding sources, amounted to $7.400 billion at June 30, 2013 versus $8.177 billion at December 31, 2012, an 9.5% decrease.

At June 30, 2013, deposits represented 77% and borrowings represented 23% of interest-bearing liabilities, compared to 70% and 30%, respectively, at December 31, 2012. At June 30, 2013, deposits and accrued interest payable, the largest category of the Company's interest-bearing liabilities, were $5.665 billion, down 0.4% from $5.690 billion at December 31, 2012. Core deposits increased 2.7% to $4.891 billion at June 30, 2013 from December 31, 2012, and brokered deposits decreased 16.6% to $774.1 million as of June 30, 2013 from $928.2 million at December 31, 2012.

Borrowings consist mainly of funding sources through the use of repurchase agreements, FHLB advances, subordinated capital notes, and short-term borrowings. At June 30, 2013, borrowings amounted to $1.735 billion, 30.3% lower than the $2.488 billion reported at December 31, 2012. Repurchase agreements as of June 30, 2013 decreased $381.4 million to $1.314 billion from $1.695 billion at December 31, 2012, as the Company used available cash to pay off repurchase agreements at maturity.

As a member of the FHLB, the Bank can obtain advances from the FHLB, secured by the FHLB stock owned by the Bank, as well as by certain of the Bank's mortgage loans and investment securities. Advances from FHLB amounted to $285.1 million and $536.5 million as of June 30, 2013 and December 31, 2012, respectively. These advances mature from July 2013 through January 2018.

Stockholders' Equity

At June 30, 2013, the Company's total stockholders' equity was $870.9 million, a 0.8% increase when compared to $863.6 million at December 31, 2012. Increase in stockholders' equity was mainly driven by the income for the six-month period, partially offset by changes to other comprehensive income.

Tangible common equity to total assets increased to 7.30% from 6.74% at the end of the last year. Tier 1 Leverage Capital Ratio increased to 8.54% from 6.42%, Tier 1 Risk-Based Capital Ratio increased to 13.96% from 12.94%, and Total Risk-Based Capital Ratio increased to 16.02% from 15.15% on December 31, 2012.

The Company maintains capital ratios in excess of regulatory requirements. At June 30, 2013, Tier 1 Leverage Capital Ratio was 2.14 times the minimum requirement of 4.00%, Tier 1 Risk-Based Capital Ratio was 3.49 times the minimum requirement of 4.00%, and Total Risk-Based Capital Ratio was 2.00 times the minimum requirement of 8.00%.

The following are the consolidated capital ratios of the Company at June 30, 2013 and December 31, 2012:

TABLE 7 — CAPITAL, DIVIDENDS AND STOCK DATA

	June 30, 2013	December 31, 2012	Variance %
	(Dollars in thousands, except per share data)		
Capital data:			
Stockholders' equity	$ 870,924	$ 863,606	0.8%
Regulatory Capital Ratios data:			
Leverage capital ratio	**8.54%**	**6.42%**	32.9%
Minimum leverage capital ratio required	4.00%	4.00%	
Actual tier 1 capital	$ 702,801	$ 678,127	3.6%
Minimum tier 1 capital required	$ 329,225	$ 422,307	-22.0%
Excess over regulatory requirement	$ 373,576	$ 255,820	46.0%
Tier 1 risk-based capital ratio	**13.96%**	**12.94%**	7.9%
Minimum tier 1 risk-based capital ratio required	4.00%	4.00%	
Actual tier 1 risk-based capital	$ 702,801	$ 678,127	3.6%
Minimum tier 1 risk-based capital required	$ 201,409	$ 209,634	-3.9%
Excess over regulatory requirement	$ 501,392	$ 468,493	7.0%
Risk-weighted assets	$ 5,035,233	$ 5,240,861	-3.9%
Total risk-based capital ratio	**16.02%**	**15.15%**	5.7%
Minimum total risk-based capital ratio required	8.00%	8.00%	
Actual total risk-based capital	$ 806,418	$ 794,195	1.5%
Minimum total risk-based capital required	$ 402,819	$ 419,269	-3.9%
Excess over regulatory requirement	$ 403,599	$ 374,926	7.6%
Risk-weighted assets	$ 5,035,233	$ 5,240,861	-3.9%
Tangible common equity to total assets	**7.30%**	**6.73%**	8.5%
Tangible common equity to risk-weighted assets	**12.22%**	**11.82%**	3.4%
Total equity to total assets	**10.32%**	**9.39%**	9.9%
Total equity to risk-weighted assets	**17.30%**	**16.48%**	5.0%
Tier 1 common equity to risk-weighted assets	**9.97%**	**9.11%**	9.4%
Tier 1 common equity capital	$ 501,932	$ 477,241	5.2%
Stock data:			
Outstanding common shares	45,640,105	45,580,281	0.1%

Book value per common share	$	15.45	$	15.31	0.9%
Market price at end of period	$	18.11	$	13.35	35.7%
Market capitalization at end of period	$	826,542	$	608,497	35.8%

	Six-Month Period Ended June 30,				
		2013		2012	Variance %
Common dividend data:					
Cash dividends declared	$	5,479	$	4,886	12.1%
Cash dividends declared per share	$	0.12	$	0.12	0.0%
Payout ratio		11.54%		21.19%	-45.5%
Dividend yield		1.33%		2.17%	-38.9%

The following table presents a reconciliation of the Company's total stockholders' equity to tangible common equity and total assets to tangible assets at June 30, 2013 and December 31, 2012:

	June 30, 2013	December 31, 2012
	(In thousands, except share or per share information)	
Total stockholders' equity	$ 870,924	$ 863,606
Preferred stock	(176,000)	(176,000)
Preferred stock issuance costs	10,130	10,115
Goodwill	(76,383)	(76,383)
Core deposit intangible	(8,633)	(9,463)
Customer relationship intangible	(4,568)	(5,027)
Total tangible common equity	**$ 615,470**	**$ 606,848**
Total assets	8,435,934	9,196,261
Goodwill	(76,383)	(76,383)
Core deposit intangible	(8,633)	(9,463)
Customer relationship intangible		