IV. Financial Statements and Notes

Deposit Insurance Fund

Federal Deposit Insurance Corporation

Deposit Insurance Fund Balance Sheet at December 31

Dollars in Thousands

	2007	2006
Assets		
Cash and cash equivalents	$ 4,244,547	$ 2,953,995
Investment in U.S. Treasury obligations, net: (Note 3)		
Held-to-maturity securities	38,015,174	37,184,214
Available-for-sale securities	8,572,800	8,958,566
Assessments receivable, net (Note 7)	244,581	0
Interest receivable on investments and other assets, net	768,292	747,715
Receivables from resolutions, net (Note 4)	808,072	538,991
Property and equipment, net (Note 5)	351,861	376,790
Total Assets	**$ 53,005,327**	**$ 50,760,271**
Liabilities		
Accounts payable and other liabilities	$ 151,857	$ 154,283
Postretirement benefit liability (Note 11)	116,158	129,906
Contingent liabilities for: (Note 6)		
Anticipated failure of insured institutions	124,276	110,775
Litigation losses	200,000	200,000
Total Liabilities	**592,291**	**594,964**
Commitments and off-balance-sheet exposure (Note 12)		
Fund Balance		
Accumulated net income	52,034,503	49,929,226
Unrealized gain on available-for-sale securities, net (Note 3)	358,908	233,822
Unrealized postretirement benefit gain (Note 11)	19,625	2,259
Total Fund Balance	**52,413,036**	**50,165,307**
Total Liabilities and Fund Balance	**$ 53,005,327**	**$ 50,760,271**

The accompanying notes are an integral part of these financial statements.

Federal Deposit Insurance Corporation

Deposit Insurance Fund Statement of Income and Fund Balance for the Years Ended December 31

Dollars in Thousands

	2007	2006
Revenue		
Interest on U.S. Treasury obligations	$ 2,540,061	$ 2,240,723
Assessments (Note 7)	642,928	31,945
Exit fees earned (Note 8)	0	345,295
Other revenue	13,244	25,565
Total Revenue	**3,196,233**	**2,643,528**
Expenses and Losses		
Operating expenses (Note 9)	992,570	950,618
Provision for insurance losses (Note 10)	95,016	(52,097)
Insurance and other expenses	3,370	5,843
Total Expenses and Losses	**1,090,956**	**904,364**
Net Income	**2,105,277**	**1,739,164**
Unrealized gain/(loss) on available-for-sale securities, net (Note 3)	125,086	(172,718)
Unrealized postretirement benefit gain (Note 11)	17,366	2,259
Comprehensive Income	**2,247,729**	**1,568,705**
Fund Balance - Beginning	**50,165,307**	**48,596,602**
Fund Balance - Ending	**$ 52,413,036**	**$ 50,165,307**

The accompanying notes are an integral part of these financial statements.

Federal Deposit Insurance Corporation

Deposit Insurance Fund Statement of Cash Flows for the Years Ended December 31

Dollars in Thousands

	2007	2006
Operating Activities		
Net Income:	$ 2,105,277	$ 1,739,164
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of U.S. Treasury obligations	571,267	599,274
Treasury inflation-protected securities (TIPS) inflation adjustment	(313,836)	(109,394)
Depreciation on property and equipment	63,115	52,919
Loss on retirement of property and equipment	153	0
Provision for insurance losses	95,016	(52,097)
Terminations/adjustments of work-in-process accounts	0	433
Exit fees earned	0	(345,295)
Unrealized gain on postretirement benefits	17,366	0
Change in Operating Assets and Liabilities:		
Decrease in unamortized premium and discount of U.S. Treasury obligations (restricted)	0	1,359
(Increase) in assessments receivable, net	(244,581)	0
(Increase) in interest receivable and other assets	(20,442)	(14,635)
(Increase)/Decrease in receivables from resolutions	(350,309)	147,258
(Decrease) in accounts payable and other liabilities	(39,580)	(166,822)
(Decrease)/Increase in postretirement benefit liability	(13,748)	129,906
Increase in exit fees and investment proceeds held in escrow	0	3,639
Net Cash Provided by Operating Activities	**1,869,698**	**1,985,709**
Investing Activities		
Provided by:		
Maturity of U.S. Treasury obligations, held-to-maturity	6,401,000	5,955,000
Maturity of U.S. Treasury obligations, available-for-sale	1,225,000	845,000
Used by:		
Purchase of property and equipment	(1,607)	(11,721)
Purchase of U.S. Treasury obligations, held-to-maturity	(7,706,117)	(9,050,372)
Purchase of U.S. Treasury obligations, available-for-sale	(497,422)	0
Net Cash Used by Investing Activities	**(579,146)**	**(2,262,093)**
Net Increase/(Decrease) in Cash and Cash Equivalents	**1,290,552**	**(276,384)**
Cash and Cash Equivalents - Beginning	**2,953,995**	**3,230,379**
Cash and Cash Equivalents - Ending	**$ 4,244,547**	**$ 2,953,995**

The accompanying notes are an integral part of these financial statements.

Notes to the Financial Statements
December 31, 2007 and 2006

1 Legislation and Operations of the Deposit Insurance Fund

Overview

The Federal Deposit Insurance Corporation (FDIC) is the independent deposit insurance agency created by Congress in 1933 to maintain stability and public confidence in the nation's banking system. Provisions that govern the operations of the FDIC are generally found in the Federal Deposit Insurance (FDI) Act, as amended, (12 U.S.C. 1811, *et seq*). In carrying out the purposes of the FDI Act, as amended, the FDIC insures the deposits of banks and savings associations (insured depository institutions), and in cooperation with other federal and state agencies promotes the safety and soundness of insured depository institutions by identifying, monitoring and addressing risks to the deposit insurance fund. An active institution's primary federal supervisor is generally determined by the institution's charter type. Commercial and savings banks are supervised by the FDIC, the Office of the Comptroller of the Currency, or the Federal Reserve Board, while thrifts are supervised by the Office of Thrift Supervision.

The Deposit Insurance Fund (DIF) was established on March 31, 2006, as a result of the merger of the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF). The FDIC is the administrator of the DIF and the FSLIC Resolution Fund (FRF). These funds are maintained separately to carry out their respective mandates.

The DIF is an insurance fund responsible for protecting insured bank and thrift depositors from loss due to institution failures. The FRF is a resolution fund responsible for the sale of remaining assets and satisfaction of liabilities associated with the former Federal Savings and Loan Insurance Corporation (FSLIC) and the Resolution Trust Corporation.

Recent Legislation

The Federal Deposit Insurance Reform Act of 2005 (Title II, Subtitle B of Public Law 109-171, 120 Stat. 9) and the Federal Deposit Insurance Reform Conforming Amendments Act of 2005 (Public Law 109-173, 119 Stat. 3601) were enacted in February 2006. Pursuant to this legislation (collectively, the Reform Act), the BIF and the SAIF were merged as discussed above. Additionally, as a result of the Reform Act, the FDIC immediately increased coverage for certain retirement accounts to $250,000 and required the deposit of funds into the DIF for SAIF-member exit fees that had been restricted and held in escrow. Furthermore, the Reform Act: 1) provides the FDIC with greater discretion to charge insurance assessments and to impose more sensitive risk-based pricing; 2) annually permits the designated reserve ratio to vary between 1.15 and 1.50 percent of estimated insured deposits, thereby eliminating the statutorily fixed designated reserve ratio of 1.25 percent; 3) generally requires the declaration and payment of dividends from the DIF if the reserve ratio of the DIF equals or exceeds 1.35 percent of estimated insured deposits at the end of a calendar year; 4) grants a one-time assessment credit for each eligible insured depository institution or its successor based on an institution's proportionate share of the aggregate assessment base of all eligible institutions at December 31, 1996; and 5) allows the FDIC to increase all deposit insurance coverage, under certain circumstances, to reflect inflation every five years beginning January 1, 2011. See Note 7 for additional discussion on the reforms related to Assessments.

Operations of the DIF

The primary purpose of the DIF is to: 1) insure the deposits and protect the depositors of DIF-insured institutions and 2) resolve DIF-insured failed institutions upon appointment of FDIC as receiver in a manner that will result in the least possible cost to the DIF.

The DIF is primarily funded from: 1) interest earned on investments in U.S. Treasury obligations and 2) deposit insurance assessments. Additional funding sources, if necessary, are borrowings from the U.S. Treasury, Federal Financing Bank, Federal Home Loan Banks, and insured depository institutions. The FDIC has borrowing authority from the U.S. Treasury up to $30 billion and a Note Purchase Agreement with the Federal Financing Bank not to exceed $40 billion to enhance DIF's ability to fund deposit insurance obligations.

A statutory formula, known as the Maximum Obligation Limitation (MOL), limits the amount of obligations the DIF can incur to the sum of its cash, 90 percent of the fair market value of other assets, and the amount authorized to be borrowed from the U.S. Treasury. The MOL for the DIF was $83.6 billion and $79.7 billion as of December 31, 2007 and 2006, respectively.

Receivership Operations

The FDIC is responsible for managing and disposing of the assets of failed institutions in an orderly and efficient manner. The assets held by receivership entities, and the claims against them, are accounted for separately from DIF assets and liabilities to ensure that receivership proceeds are distributed in accordance with applicable laws and regulations. Accordingly, income and expenses attributable to receiverships are accounted for as transactions of those receiverships. Receiverships are billed by the FDIC for services provided on their behalf.

2 Summary of Significant Accounting Policies

General

These financial statements pertain to the financial position, results of operations, and cash flows of the DIF and are presented in conformity with U.S. generally accepted accounting principles (GAAP). These statements do not include reporting for assets and liabilities of closed banks and thrifts for which the FDIC acts as receiver. Periodic and final accountability reports of the FDIC's activities as receiver are furnished to courts, supervisory authorities, and others as required.

Use of Estimates

Management makes estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. Where it is reasonably possible that changes in estimates will cause a material change in the financial statements in the near term, the nature and extent of such changes in estimates have been disclosed. The more significant estimates include the assessments receivable and associated revenue, the allowance for loss on receivables from resolutions, the estimated losses for anticipated failures and litigation, and the postretirement benefit obligation.

Cash Equivalents

Cash equivalents are short-term, highly liquid investments with original maturities of three months or less. Cash equivalents consist primarily of Special U.S. Treasury Certificates.

Investment in U.S. Treasury Obligations

DIF funds are required to be invested in obligations of the United States or in obligations guaranteed as to principal and interest by the United States; the Secretary of the U.S. Treasury must approve all such investments in excess of $100,000. The Secretary has granted approval to invest DIF funds only in U.S. Treasury obligations that are purchased or sold exclusively through the Bureau of the Public Debt's Government Account Series (GAS) program.

DIF's investments in U.S. Treasury obligations are either classified as held-to-maturity or available-for-sale based on the FDIC's assessment of funding needs. Securities designated as held-to-maturity are shown at amortized cost. Amortized cost is the face value of securities plus the unamortized premium or less the unamortized discount. Amortizations are computed on a daily basis from the date of acquisition to the date of maturity, except for callable U.S. Treasury securities, which are amortized to the first call date. Securities designated as available-for-sale are shown at market value, which approximates fair value. Unrealized gains and losses are included in Comprehensive Income. Realized gains and losses are included in the Statement of Income and Fund Balance as components of Net Income. Income on both types of securities is calculated and recorded on a daily basis using the effective interest method.

Revenue Recognition for Assessments

Prior to 2007, insurance assessments were fully paid in advance on the last day of each quarter for the next quarter and recorded as unearned assessment revenue. One-third of the amount was recognized monthly as assessment income during the quarter in accordance with GAAP.

The Reform Act granted the FDIC discretion in the manner assessments are determined and collected from insured depository institutions. As a result, the FDIC now collects deposit insurance premiums at the end of the quarter following the period of insurance coverage. Consequently, assessment revenue for the insured period is recognized based on an estimate. The estimate is derived from an institution's risk-based assessment rate and assessment base for the prior quarter; adjusted for the current quarter's available assessment credits, any changes in supervisory examination and debt issuer ratings for larger institutions, and a modest deposit insurance growth factor.

The estimated revenue amounts are adjusted when actual premiums are collected at quarter end. Total assessment income recognized for the year includes estimated revenue for the October-December assessment period. See Note 7 for additional information on assessments.

Capital Assets and Depreciation

The FDIC buildings are depreciated on a straight-line basis over a 35 to 50 year estimated life. Leasehold improvements are capitalized and depreciated over the lesser of the remaining life of the lease or the estimated useful life of the improvements, if determined to be material. Capital assets depreciated on a straight-line basis over a five-year estimated life include mainframe equipment; furniture, fixtures, and general equipment; and internal-use software. Personal computer equipment is depreciated on a straight-line basis over a three-year estimated life.

Disclosure about Recent Accounting Pronouncements

The Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, in September 2006. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. The Statement does not require any new fair value measurements. FDIC will adopt SFAS No. 157 effective January 1, 2008, on a prospective basis. Management does not expect the Statement to have a material impact on the financial statements.

Related Parties

The nature of related parties and a description of related party transactions are discussed in Note 1 and disclosed throughout the financial statements and footnotes.

3 Investment in U.S. Treasury Obligations, Net

As of December 31, 2007 and 2006, investments in U.S. Treasury obligations, net, were $46.6 billion and $46.1 billion, respectively. As of December 31, 2007, the DIF held $9.6 billion of Treasury inflation-protected securities (TIPS). These securities are indexed to increases or decreases in the Consumer Price Index for All Urban Consumers (CPI-U). Additionally, the DIF held $4.3 billion of callable U.S. Treasury bonds at December 31, 2007. Callable U.S. Treasury bonds may be called five years prior to the respective bonds' stated maturity on their semi-annual coupon payment dates upon 120 days notice.

U.S. Treasury Obligations at December 31, 2007

Dollars in Thousands

Maturity•	Yield at Purchase▼	Face Value	Net Carrying Amount	Unrealized Holding Gains	Unrealized Holding Losses■	Market Value
Held-to-Maturity						
U.S. Treasury notes and bonds						
Within 1 year	4.49%	$ 5,600,000	$ 5,651,699	$ 30,313	$ (469)	$ 5,681,543
After 1 year thru 5 years	4.50%	12,920,000	13,310,856	416,031	0	13,726,887
After 5 years thru 10 years	4.81%	11,550,000	12,856,888	764,723	0	13,621,611
After 10 years	5.02%	3,500,000	4,626,945	286,889	0	4,913,834
U.S. Treasury inflation-protected securities						
Within 1 year	3.86%	258,638	258,620	349	0	258,969
After 1 year thru 5 years	3.16%	$ 1,288,950	$ 1,310,166	$ 52,927	$ 0	$ 1,363,093
Total		**$ 35,117,588**	**$ 38,015,174**	**$ 1,551,232**	**$ (469)**	**$ 39,565,937**
Available-for-Sale						
U.S. Treasury notes and bonds						
After 1 year thru 5 years	4.79%	$ 500,000	$ 498,260	$ 10,100	$ 0	$ 508,360
U.S. Treasury inflation-protected securities						
Within 1 year	3.92%	1,700,545	1,700,397	2,325	0	1,702,722
After 1 year thru 5 years	3.75%	6,004,277	6,015,235	346,483	0	6,361,718
Total		**$ 8,204,822**	**$ 8,213,892**	**$ 358,908**	**$ 0**	**$ 8,572,800**
Total Investment in U.S. Treasury Obligations, Net						
Total		**$ 43,322,410**	**$ 46,229,066**	**$ 1,910,140**	**$ (469)**	**$ 48,138,737**

• For purposes of this table, all callable securities are assumed to mature on their first call dates. Their yields at purchase are reported as their yield to first call date.

▼ For TIPS, the yields in the above table are stated at their real yields at purchase, not their effective yields. Effective yields on TIPS include a long-term annual inflation assumption as measured by the CPI-U. The long-term CPI-U consensus forecast is 2.2 percent, based on figures issued by the Congressional Budget Office and *Blue Chip Economic Indicators* in early 2007.

■ All unrealized losses occurred as a result of changes in market interest rates. FDIC has the ability and intent to hold the related securities until maturity. As a result, all unrealized losses are considered temporary. However, all of the $469 thousand reported as total unrealized losses is recognized as unrealized losses occurring over a period of 12 months or longer with a market value of $1.1 billion applied to the affected securities.

U.S. Treasury Obligations at December 31, 2006

Dollars in Thousands

Maturity[•]	Yield at Purchase[▾]	Face Value	Net Carrying Amount	Unrealized Holding Gains	Unrealized Holding Losses[■]	Market Value
Held-to-Maturity						
U. S. Treasury notes and bonds						
Within 1 year	4.58%	$ 6,401,000	$ 6,448,905	$ 3,389	$ (20,704)	$ 6,431,590
After 1 year thru 5 years	4.47%	15,500,000	16,276,424	91,703	(196,635)	16,171,492
After 5 years thru 10 years	4.68%	9,025,000	9,690,085	36,025	(42,270)	9,683,840
After 10 years	5.01%	2,445,000	3,247,814	57,589	(3,227)	3,302,176
U. S. Treasury inflation-protected securities						
After 1 year thru 5 years	3.83%	926,751	926,844	21,185	0	948,029
After 5 years thru 10 years	2.41%	568,345	594,142	0	(778)	593,364
Total		**$ 34,866,096**	**$ 37,184,214**	**$ 209,891**	**$ (263,614)**	**$ 37,130,491**
Available-for-Sale						
U. S. Treasury notes and bonds						
Within 1 year	3.85%	$ 1,225,000	$ 1,269,835	$ 0	$ (9,208)	$ 1,260,627
U. S. Treasury inflation-protected securities						
After 1 year thru 5 years	3.80%	7,443,478	7,454,909	243,030	0	7,697,939
Total		**$ 8,668,478**	**$ 8,724,744**	**$ 243,030**	**$ (9,208)**	**$ 8,958,566**
Total Investment in U.S. Treasury Obligations, Net						
Total		**$ 43,534,574**	**$ 45,908,958**	**$ 452,921**	**$ (272,822)**	**$ 46,089,057**

• For purposes of this table, all callable securities are assumed to mature on their first call dates. Their yields at purchase are reported as their yield to first call date.

▾ For TIPS, the yields in the above table are stated at their real yields at purchase, not their effective yields. Effective yields on TIPS include a long-term annual inflation assumption as measured by the CPI-U. The long-term CPI-U consensus forecast is 2.2 percent, based on figures issued by the Congressional Budget Office and *Blue Chip Economic Indicators* in early 2006.

■ All unrealized losses occurred as a result of changes in market interest rates. FDIC has the ability and intent to hold the related securities until maturity. As a result, all unrealized losses are considered temporary. However, of the $273 million reported as total unrealized losses, $237 million is recognized as unrealized losses occurring over a period of 12 months or longer with a market value of $13.3 billion applied to the affected securities.

As of December 31, 2007 and 2006, the unamortized premium, net of the unamortized discount, was $2.9 billion and $2.4 billion, respectively.

4 Receivables From Resolutions, Net

The receivables from resolutions include payments made by the DIF to cover obligations to insured depositors, advances to receiverships for working capital, and administrative expenses paid on behalf of receiverships. Any related allowance for loss represents the difference between the funds advanced and/or obligations incurred and the expected repayment. Assets held by DIF receiverships are the main source of repayment of the DIF's receivables from closed banks and thrifts. As of December 31, 2007, there were 22 active receiverships, including three failures in the current year.

As of December 31, 2007 and 2006, DIF receiverships held assets with a book value of $1.2 billion and $655 million, respectively (including cash, investments, and miscellaneous receivables of $363 million and $348 million at December 31, 2007 and 2006, respectively). The estimated cash recoveries from the management and disposition of assets that are used to derive the allowance for losses are based on a sampling of receivership assets in liquidation. Sampled assets were generally valued by estimating future cash recoveries, net of applicable liquidation cost estimates, and then discounted using current market-based risk factors applicable to a given asset's type and quality. Resultant recovery estimates were extrapolated to the non-sampled assets in order to derive the allowance for loss on the receivable. Estimated asset recoveries are regularly evaluated, but remain subject to uncertainties because of potential changes in economic and market conditions. Such uncertainties could cause the DIF's actual recoveries to vary from current estimates.

Receivables From Resolutions, Net at December 31

Dollars in Thousands

	2007	2006
Receivables from closed banks	$ 4,991,003	$ 4,650,025
Allowance for losses	(4,182,931)	(4,111,034)
Total	**$ 808,072**	**$ 538,991**

As of December 31, 2007, the DIF allowance for loss was $4.18 billion, representing 84 percent of the gross receivable. Of the remaining 16 percent of the gross receivable, the amount of credit risk is limited since 60 percent of the $808 million net receivable will be repaid from receivership cash, investments, and a promissory note fully secured by a letter of credit. The majority of the remaining 40 percent will be repaid from assets classified as or supported by real estate mortgages. Although estimated asset recoveries are regularly evaluated, the impact of any additional credit risk exposure, due to ongoing conditions in the housing market, is uncertain at this time.

5 Property and Equipment, Net

Property and Equipment, Net at December 31

Dollars in Thousands

	2007	2006
Land	$ 37,352	$ 37,352
Buildings (including leasehold improvements)	276,626	284,871
Application software (includes work-in-process)	145,693	232,206
Furniture, fixtures, and equipment	71,138	145,635
Accumulated depreciation	(178,948)	(323,274)
Total	**$ 351,861**	**$ 376,790**

The depreciation expense was $63 million and $53 million for December 31, 2007 and 2006, respectively.

6 Contingent Liabilities for:

Anticipated Failure of Insured Institutions

The DIF records a contingent liability and a loss provision for DIF-insured institutions that are likely to fail within one year of the reporting date, absent some favorable event such as obtaining additional capital or merging, when the liability becomes probable and reasonably estimable.

The contingent liability is derived by applying expected failure rates and loss rates to institutions based on supervisory ratings, balance sheet characteristics, and projected capital levels. In addition, institution-specific analysis is performed on those institutions where failure is imminent absent institution management resolution of existing problems, or where additional information is available that may affect the estimate of losses. As of December 31, 2007 and 2006, the contingent liabilities for anticipated failure of insured institutions were $124.3 million and $110.8 million, respectively, including an estimated liability for one small institution that failed on January 25, 2008.

In addition to these recorded contingent liabilities, the FDIC has identified additional risk in the financial services industry that could result in an additional loss to the DIF should potentially vulnerable insured institutions ultimately fail. As a result of these risks, the FDIC believes that it is reasonably possible that the DIF could incur additional estimated losses up to approximately $1.7 billion. The actual losses if any will largely depend on future economic and market conditions and could differ materially from this estimate.

During 2007, an increasingly difficult economic and credit environment challenged the soundness and profitability of some FDIC-insured institutions. The downturn in housing markets led to asset-quality problems and volatility in financial markets, which hurt banking industry performance and threatened the viability of some institutions that had significant exposure to higher risk residential mortgages. It is uncertain how long the effects of this downturn will last. While supervisory and market data suggest that the banking industry will continue to experience elevated levels of stress over the coming year, as of September 30, 2007, 99% of insured institutions met the highest regulatory capital ("well capitalized") standard. The FDIC continues to evaluate the risks to affected institutions in light of evolving economic conditions; however, the impact of such risks on the insurance fund cannot be reasonably estimated at this time.

Litigation Losses

The DIF records an estimated loss for unresolved legal cases to the extent that those losses are considered probable and reasonably estimable. In addition to the $200 million recorded as probable, the FDIC has determined that losses from unresolved legal cases totaling $0.6 million are reasonably possible.

Other Contingencies

Representations and Warranties

As part of the FDIC's efforts to maximize the return from the sale of assets from bank and thrift resolutions, representations and warranties, and guarantees were offered on certain loan sales. In general, the guarantees, representations, and warranties on loans sold relate to the completeness and accuracy of loan documentation, the quality of the underwriting standards used, the accuracy of the delinquency status when sold, and the conformity of the loans with characteristics of the pool in which they were sold. The total amount of loans sold subject to unexpired representations and warranties, and guarantees was $8.1 billion as of December 31, 2007. There were no contingent liabilities from any of the outstanding claims asserted in connection with representations and warranties at December 31, 2007 and 2006, respectively.

In addition, future losses could be incurred until the contracts offering the representations and warranties, and guarantees have expired, some as late as 2032. Consequently, the FDIC believes it is possible that additional losses may be incurred by the DIF from the universe of outstanding contracts with unasserted representation and warranty claims. However, because of the uncertainties surrounding the timing of when claims may be asserted, the FDIC is unable to reasonably estimate a range of loss to the DIF from outstanding contracts with unasserted representation and warranty claims.

7 Assessments

The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) required the FDIC to establish a risk-based assessment system, charging higher rates to those insured depository institutions that posed greater risks to the DIF. To arrive at a risk-based assessment for a particular institution, the FDIC placed each institution in one of nine risk categories based on capital ratios and supervisory examination data. Based on FDIC's evaluation of the institutions under the risk-based premium system and due to the limitations imposed by the Deposit Insurance Funds Act of 1996 (DIFA) and the health of the banking and thrift industries, most institutions were not charged an assessment for a number of years. In addition, the FDIC was required by statute to maintain the insurance funds at a designated reserve ratio (DRR) of not less than 1.25 percent of estimated insured deposits (or a higher percentage as circumstances warranted).

Effective January 1, 2007, the Reform Act continues to require a risk-based assessment system and allows the FDIC discretion in defining risk. By regulation, the FDIC has consolidated the number of assessment risk categories from nine to four. The four new categories continue to be defined based upon supervisory and capital evaluations. Other significant changes mandated by the Reform Act and the implementing regulations:

- require payment of assessments by all insured depository institutions, eliminating the restriction on assessments for the best-rated institutions;
- grant a one-time assessment credit of approximately $4.7 billion to certain eligible insured depository institutions (or their successors) based on the assessment base of the institution as of December 31, 1996, as compared to the combined aggregate assessment base of all eligible institutions;
- establish a range for the DRR from 1.15 to 1.50 percent of estimated insured deposits and eliminate the fixed DRR of 1.25 percent. The FDIC is required to annually publish the DRR and has, by regulation, set the DRR at 1.25 percent for 2008. As of September 30, 2007, the DIF reserve ratio was 1.22% of estimated insured deposits;
- require the FDIC to adopt a DIF restoration plan to return the reserve ratio to 1.15 percent generally within five years, if the reserve ratio falls below 1.15 percent or is expected to fall below 1.15 percent within six months;
- require the FDIC to annually determine if a dividend should be paid, based on the statutory requirement generally to declare dividends if the reserve ratio exceeds 1.35 percent at the end of a calendar year. The Reform Act permits dividends for one-half of the amount required to maintain the reserve ratio at 1.35 percent when the reserve ratio is between 1.35 and 1.50 percent and all amounts required to maintain the reserve ratio at 1.50 percent when the reserve ratio exceeds 1.50 percent.

The assessment rate averaged approximately 5.4 cents and .05 cents per $100 of assessable deposits for 2007 and 2006, respectively. At December 31, 2007, the "Assessments Receivable, net" line item of $245 million represents the estimated gross premiums due from insured depository institutions for the fourth quarter of the year, net of $708 million in estimated one-time assessment credits. The actual deposit insurance assessments for the fourth quarter will be billed and collected at the end of the first quarter of 2008. During 2007 and 2006, $643 million and $32 million were recognized as assessment income from institutions, respectively.

Assessments Revenue for the Year Ended December 31

Dollars in Thousands

	2007
Gross assessments	$ 3,730,886
Less: One-time assessment credits applied	(3,087,958)
Assessments Revenue	**$ 642,928**

Of the $4.7 billion in one-time assessment credits granted, $1.6 billion (34 percent) remained as of December 31, 2007. The use of assessment credits is limited to no more than 90 percent of the gross assessments for assessment periods that provide deposit insurance coverage in years 2008 through 2010. Credits are also restricted when the reserve ratio is less than 1.15 percent and for institutions that are not adequately capitalized or exhibit financial, operational or compliance weaknesses. The credits can only be used to offset future deposit insurance assessments and, therefore, do not represent a liability to the DIF. They are transferable among institutions, do not expire, and cannot be used to offset Financing Corporation (FICO) payments.

Assessments continue to be levied on institutions for payments of the interest on obligations issued by the FICO. The FICO was established as a mixed-ownership government corporation to function solely as a financing vehicle for the FSLIC. The annual FICO interest obligation of approximately $790 million is paid on a pro rata basis using the same rate for banks and thrifts. The FICO assessment has no financial impact on the DIF and is separate from deposit insurance assessments. The FDIC, as administrator of the DIF, acts solely as a collection agent for the FICO. During 2007 and 2006, $785 million and $788 million, respectively, were collected and remitted to the FICO.

8 Exit Fees Earned

From the early to mid-1990s, the SAIF collected entrance and exit fees for conversion transactions when an insured depository institution converted from the BIF to the SAIF (resulting in an entrance fee) or from the SAIF to the BIF (resulting in an exit fee). The exit fees and interest earned were held in escrow pending determination of ownership. As a result, the SAIF did not recognize exit fees or any interest earned as revenue. The Reform Act removed the restriction on SAIF-member exit fees held in escrow and the funds were deposited into the general (unrestricted) fund of the DIF. The exit fees plus earned interest, a total of $345 million, were recognized as revenue at their carrying value for 2006.

9 Operating Expenses

Operating expenses were $993 million for 2007, compared to $951 million for 2006. The chart below lists the major components of operating expenses.

Operating Expenses for the Years Ended December 31

Dollars in Thousands

	2007	2006
Salaries and benefits	$ 640,294	$ 619,452
Outside services	137,812	124,045
Travel	55,281	49,408
Buildings and leased space	61,377	65,929
Software/Hardware maintenance	28,542	27,139
Depreciation of property and equipment	63,115	52,919
Other	23,640	22,124
Services billed to receiverships	(17,491)	(10,398)
Total	**$ 992,570**	**$ 950,618**

10 Provision for Insurance Losses

Provision for insurance losses was a positive $95 million for 2007 and a negative $52 million for 2006. The following chart lists the major components of the provision for insurance losses.

Provision for Insurance Losses for the Years Ended December 31

Dollars in Thousands

	2007	2006
Valuation Adjustments		
Closed banks and thrifts	$ 81,229	$ (152,776)
Other assets	286	(4,230)
Total Valuation Adjustments	**81,515**	**(157,006)**
Contingent Liabilities Adjustments:		
Anticipated failure of insured institutions	13,501	105,409
Litigation losses	0	(500)
Total Contingent Liabilities Adjustments	**13,501**	**104,909**
Total	**$ 95,016**	**$ (52,097)**

11 Employee Benefits

Pension Benefits and Savings Plans

Eligible FDIC employees (permanent and term employees with appointments exceeding one year) are covered by the federal government retirement plans, either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Although the DIF contributes a portion of pension benefits for eligible employees, it does not account for the assets of either retirement system. The DIF also does not have actuarial data for accumulated plan benefits or the unfunded liability relative to eligible employees. These amounts are reported on and accounted for by the U.S. Office of Personnel Management (OPM).

Eligible FDIC employees also may participate in a FDIC-sponsored tax-deferred 401(k) savings plan with matching contributions up to five percent. Under the Federal Thrift Savings Plan (TSP), FDIC provides FERS employees with an automatic contribution of 1 percent of pay and an additional matching contribution up to 4 percent of pay. CSRS employees also can contribute to the TSP. However, CSRS employees do not receive agency matching contributions.

Pension Benefits and Savings Plans Expenses for the Years Ended December 31

Dollars in Thousands

	2007	2006
Civil Service Retirement System	$ 6,698	$ 6,808
Federal Employees Retirement System (Basic Benefit)	40,850	38,915
FDIC Savings Plan	21,008	20,681
Federal Thrift Savings Plan	15,938	15,328
Severance Pay	59	39
Total	**$ 84,553**	**$ 81,771**

Postretirement Benefits Other Than Pensions

The DIF has no postretirement health insurance liability, since all eligible retirees are covered by the Federal Employees Health Benefit (FEHB) program. FEHB is administered and accounted for by the OPM. In addition, OPM pays the employer share of the retiree's health insurance premiums.

The FDIC provides certain life and dental insurance coverage for its eligible retirees, the retirees' beneficiaries, and covered dependents. Retirees eligible for life and dental insurance coverage are those who have qualified due to: 1) immediate enrollment upon appointment or five years of participation in the plan and 2) eligibility for an immediate annuity. The life insurance program provides basic coverage at no cost to retirees and allows converting optional coverages to direct-pay plans. For the dental coverage, retirees are responsible for a portion of the dental premium.

The DIF has elected not to fund the postretirement life and dental benefit liabilities. As a result, the DIF recognized the underfunded status (difference between the accumulated postretirement benefit obligation and the plan assets at fair value) as a liability. Since there are no plan assets, the plan's benefit liability is equal to the accumulated postretirement benefit obligation. At December 31, 2007 and 2006, the liability was $116.2 million and $129.9 million, respectively, which is recognized in the "Postretirement benefit liability" line item on the Balance Sheet. The cumulative actuarial gains/losses (changes in assumptions and plan experience) and prior service costs/credits (changes to plan provisions that increase or decrease benefits) were $19.6 million and $2.3 million at December 31, 2007 and 2006, respectively. These amounts are reported as accumulated other comprehensive income in the "Unrealized postretirement benefit gain" line item on the Balance Sheet.

The DIF's expenses for postretirement benefits for 2007 and 2006 were $7.2 million and $9.0 million, respectively, which are included in the current and prior year's operating expenses on the Statement of Income and Fund Balance. The changes in the actuarial gains/losses and prior service costs/credits for 2007 and 2006 of $17.4 million and $2.3 million, respectively, are reported as other comprehensive income in the "Unrealized postretirement benefit gain" line item. Key actuarial assumptions used in the accounting for the plan include the discount rate of 6 percent, the rate of compensation increase of 3.45 percent, and the dental coverage trend rate of 6.10 percent. The discount rate of 6 percent is based upon rates of return on high-quality fixed income investments whose cash flows match the timing and amount of expected benefit payments. For the year ended December 31, 2007, the discount rate was increased by 1.25 percent from the rate used in 2006, resulting in a decrease in the benefit liability of $24.3 million.

12 Commitments and Off-Balance-Sheet Exposure

Commitments:

Leased Space
The FDIC's lease commitments total $63.7 million for future years. The lease agreements contain escalation clauses resulting in adjustments, usually on an annual basis. The DIF recognized leased space expense of $22 million and $30 million for the periods ended December 31, 2007 and 2006, respectively.

Leased Space Commitments

Dollars in Thousands

2008	2009	2010	2011	2012	2013/Thereafter
$ 18,855	$ 15,529	$ 11,165	$ 8,488	$ 5,999	$ 3,637

Off-Balance-Sheet Exposure:

Deposit Insurance
As of September 30, 2007, the estimated insured deposits for DIF were $4.2 trillion. This estimate is derived primarily from quarterly financial data submitted by insured depository institutions to the FDIC. This estimate represents the accounting loss that would be realized if all insured depository institutions were to fail and the acquired assets provided no recoveries.

13 Disclosures About the Fair Value of Financial Instruments

Cash equivalents are short-term, highly liquid investments and are shown at fair value. The fair market value of the investment in U.S. Treasury obligations is disclosed in Note 3 and is based on current market prices. The carrying amount of interest receivable on investments, short-term receivables, and accounts payable and other liabilities approximates their fair market value, due to their short maturities and/or comparability with current interest rates.

The net receivables from resolutions primarily include the DIF's subrogated claim arising from payments to insured depositors. The receivership assets that will ultimately be used to pay the corporate subrogated claim are valued using discount rates that include consideration of market risk. These discounts ultimately affect the DIF's allowance for loss against the net receivables from resolutions. Therefore, the corporate subrogated claim indirectly includes the effect of discounting and should not be viewed as being stated in terms of nominal cash flows.

Although the value of the corporate subrogated claim is influenced by valuation of receivership assets (see Note 4), such receivership valuation is not equivalent to the valuation of the corporate claim. Since the corporate claim is unique, not intended for sale to the private sector, and has no established market, it is not practicable to estimate a fair market value.

The FDIC believes that a sale to the private sector of the corporate claim would require indeterminate, but substantial, discounts for an interested party to profit from these assets because of credit and other risks. In addition, the timing of receivership payments to the DIF on the subrogated claim does not necessarily correspond with the timing of collections on receivership assets. Therefore, the effect of discounting used by receiverships should not necessarily be viewed as producing an estimate of market value for the net receivables from resolutions.

FSLIC Resolution Fund

Federal Deposit Insurance Corporation

FSLIC Resolution Fund Balance Sheet at December 31

Dollars in Thousands

	2007	2006
Assets		
Cash and cash equivalents	$ 3,617,133	$ 3,616,466
Receivables from thrift resolutions and other assets, net (Note 3)	34,812	36,730
Receivables from U.S. Treasury for goodwill judgments (Note 4)	35,350	251,827
Total Assets	**$ 3,687,295**	**$ 3,905,023**
Liabilities		
Accounts payable and other liabilities	$ 4,276	$ 5,497
Contingent liabilities for litigation losses and other (Note 4)	35,350	279,327
Total Liabilities	**39,626**	**284,824**
Resolution Equity (Note 5)		
Contributed capital	127,417,582	127,453,996
Accumulated deficit	(123,769,913)	(123,833,797)
Total Resolution Equity	**3,647,669**	**3,620,199**
Total Liabilities and Resolution Equity	**$ 3,687,295**	**$ 3,905,023**

The accompanying notes are an integral part of these financial statements.

Federal Deposit Insurance Corporation

FSLIC Resolution Fund Statement of Income and Accumulated Deficit for the Years Ended December 31

Dollars in Thousands

	2007	2006
Revenue		
Interest on U.S. Treasury obligations	$ 156,034	$ 151,648
Other revenue	31,558	17,650
Total Revenue	**187,592**	**169,298**
Expenses and Losses		
Operating expenses	3,364	12,002
Provision for losses	(10,135)	(19,257)
Goodwill/Guarini litigation expenses (Note 4)	195,939	411,056
Recovery of tax benefits	(68,217)	(34,783)
Other expenses	2,757	2,783
Total Expenses and Losses	**123,708**	**371,801**
Net Income/(Loss)	**63,884**	**(202,503)**
Accumulated Deficit - Beginning	**(123,833,797)**	**(123,631,294)**
Accumulated Deficit - Ending	**$ (123,769,913)**	**$ (123,833,797)**

The accompanying notes are an integral part of these financial statements.

Federal Deposit Insurance Corporation

FSLIC Resolution Fund Statement of Cash Flows for the Years Ended December 31

Dollars in Thousands

	2007	2006
Operating Activities		
Net Income/(Loss)	$ 63,884	$ (202,503)
Adjustments to reconcile net income/(loss) to net cash (used by) operating activities:		
Provision for losses	(10,135)	(19,257)
Change in Operating Assets and Liabilities:		
Decrease in receivables from thrift resolutions and other assets	12,053	21,273
(Decrease) in accounts payable and other liabilities	(1,221)	(2,302)
(Decrease)/Increase in contingent liabilities for litigation losses and other	(243,977)	21,824
Net Cash Used by Operating Activities	**(179,396)**	**(180,965)**
Financing Activities		
Provided by:		
U.S.Treasury payments for goodwill litigation (Note 4)	405,063	194,728
Used by:		
Payments to Resolution Funding Corporation (Note 5)	(225,000)	0
Net Cash Provided by Financing Activities	**180,063**	**194,728**
Net Increase in Cash and Cash Equivalents	**667**	**13,763**
Cash and Cash Equivalents - Beginning	**3,616,466**	**3,602,703**
Cash and Cash Equivalents - Ending	**$ 3,617,133**	**$ 3,616,466**

The accompanying notes are an integral part of these financial statements.

Notes to the Financial Statements
December 31, 2007 and 2006

1 Legislative History and Operations/Dissolution of the FSLIC Resolution Fund

Legislative History

The Federal Deposit Insurance Corporation (FDIC) is the independent deposit insurance agency created by Congress in 1933 to maintain stability and public confidence in the nation's banking system. Provisions that govern the operations of the FDIC are generally found in the Federal Deposit Insurance (FDI) Act, as amended, (12 U.S.C. 1811, *et seq*). In carrying out the purposes of the FDI Act, as amended, the FDIC insures the deposits of banks and savings associations, and in cooperation with other federal and state agencies promotes the safety and soundness of insured depository institutions by identifying, monitoring and addressing risks to the deposit insurance funds established in the FDI Act, as amended. In addition, FDIC is charged with responsibility for the sale of remaining assets and satisfaction of liabilities associated with the former Federal Savings and Loan Insurance Corporation (FSLIC) and the Resolution Trust Corporation (RTC).

The U.S. Congress created the FSLIC through the enactment of the National Housing Act of 1934. The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) abolished the insolvent FSLIC, created the FSLIC Resolution Fund (FRF), and transferred the assets and liabilities of the FSLIC to the FRF–except those assets and liabilities transferred to the RTC–effective on August 9, 1989. Further, the FIRREA established the Resolution Funding Corporation (REFCORP) to provide part of the initial funds used by the RTC for thrift resolutions.

The RTC Completion Act of 1993 (RTC Completion Act) terminated the RTC as of December 31, 1995. All remaining assets and liabilities of the RTC were transferred to the FRF on January 1, 1996. Today, the FRF consists of two distinct pools of assets and liabilities: one composed of the assets and liabilities of the FSLIC transferred to the FRF upon the dissolution of the FSLIC (FRF-FSLIC), and the other composed of the RTC assets and liabilities (FRF-RTC). The assets of one pool are not available to satisfy obligations of the other.

Pursuant to the Federal Deposit Insurance Reform Act of 2005, the Bank Insurance Fund and the Savings Association Insurance Fund were merged into a new fund, the Deposit Insurance Fund (DIF). The FDIC is the administrator of the FRF and the DIF. These funds are maintained separately to carry out their respective mandates.

Operations/Dissolution of the FRF

The FRF will continue operations until all of its assets are sold or otherwise liquidated and all of its liabilities are satisfied. Any funds remaining in the FRF-FSLIC will be paid to the U.S. Treasury. Any remaining funds of the FRF-RTC will be distributed to the REFCORP to pay the interest on the REFCORP bonds. In addition, the FRF-FSLIC has available until expended $602.2 million in appropriations to facilitate, if required, efforts to wind up the resolution activity of the FRF-FSLIC.

The FDIC has conducted an extensive review and cataloging of FRF's remaining assets and liabilities and is continuing to explore approaches for concluding FRF's activities. Some of the issues and items that remain open in FRF are: 1) criminal restitution orders (generally have from 5 to 10 years remaining to enforce); 2) collections of settlements and judgments obtained against officers and directors and other professionals responsible for causing or contributing to thrift losses (generally have from 6 months to 12 years remaining to enforce); 3) numerous assistance agreements entered into by the former FSLIC (FRF could continue to receive tax-sharing benefits through year 2013); and 4) goodwill litigation (no final date for resolution has been established; see Note 4). The FDIC is considering whether enabling legislation or other measures may be needed to accelerate liquidation of the remaining FRF assets and liabilities. The FRF could potentially realize substantial recoveries from the tax-sharing benefits, criminal restitution orders and professional liability claims of up to $400 million; however, any associated recoveries are not reflected in FRF's financial statements given the significant uncertainties surrounding the ultimate outcome.

Receivership Operations

The FDIC is responsible for managing and disposing of the assets of failed institutions in an orderly and efficient manner. The assets held by receivership entities, and the claims against them, are accounted for separately from FRF assets and liabilities to ensure that receivership proceeds are distributed in accordance with applicable laws and regulations. Also, the income and expenses attributable to receiverships are accounted for as transactions of those receiverships. Receiverships are billed by the FDIC for services provided on their behalf.

2 Summary of Significant Accounting Policies

General

These financial statements pertain to the financial position, results of operations, and cash flows of the FRF and are presented in conformity with U.S. generally accepted accounting principles (GAAP). These statements do not include reporting for assets and liabilities of closed thrift institutions for which the FDIC acts as receiver. Periodic and final accountability reports of the FDIC's activities as receiver are furnished to courts, supervisory authorities, and others as required.

Use of Estimates

Management makes estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. Where it is reasonably possible that changes in estimates will cause a material change in the financial statements in the near term, the nature and extent of such changes in estimates have been disclosed. The more significant estimates include allowance for losses on receivables from thrift resolutions and the estimated losses for litigation.

Provision for Losses

The provision for losses represents the change in the valuation of the receivables from thrift resolutions and other assets.

Fair Value of Financial Instruments

Cash equivalents, which consist of Special U.S. Treasury Certificates, are short-term, highly liquid investments with original maturities of three months or less and are shown at fair value. The carrying amount of short-term receivables and accounts payable and other liabilities approximates their fair market value, due to their short maturities.

The net receivable from thrift resolutions is influenced by the underlying valuation of receivership assets. This corporate receivable is unique and the estimate presented is not necessarily indicative of the amount that could be realized in a sale to the private sector. Such a sale would require indeterminate, but substantial, discounts for an interested party to profit from these assets because of credit and other risks. Consequently, it is not practicable to estimate its fair market value.

Other assets primarily consist of credit enhancement reserves, which are valued by performing projected cash flow analyses using market-based assumptions (see Note 3).

Disclosure About Recent Accounting Pronouncements

The Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*, in September 2006. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. The Statement does not require any new fair value measurements. FDIC will adopt SFAS No. 157 effective January 1, 2008, on a prospective basis. Management does not expect the Statement to have a material impact on the financial statements.

Related Parties

The nature of related parties and a description of related party transactions are discussed in Note 1 and disclosed throughout the financial statements and footnotes.

3 Receivables From Thrift Resolutions and Other Assets, Net

Receivables From Thrift Resolutions

The receivables from thrift resolutions include payments made by the FRF to cover obligations to insured depositors, advances to receiverships for working capital, and administrative expenses paid on behalf of receiverships. Any related allowance for loss represents the difference between the funds advanced and/or obligations incurred and the expected repayment. Assets held by the FDIC in its receivership capacity for the former RTC are a significant source of repayment of the FRF's receivables from thrift resolutions. As of December 31, 2007, 13 of the 850 FRF receiverships remain active primarily due to unresolved litigation, including goodwill matters.

As of December 31, 2007 and 2006, FRF receiverships held assets with a book value of $22 million and $33 million, respectively (including cash, investments, and miscellaneous receivables of $18 million and $26 million at December 31, 2007 and 2006, respectively). The estimated cash recoveries from the management and disposition of these assets are used to derive the allowance for losses. The FRF receivership assets are valued by discounting projected cash flows, net of liquidation costs using current market-based risk factors applicable to a given asset's type and quality. These estimated asset recoveries are regularly evaluated, but remain subject to uncertainties because of potential changes in economic and market conditions. Such uncertainties could cause the FRF's actual recoveries to vary from current estimates.

Other Assets

Other assets primarily include credit enhancement reserves valued at $20.2 million as of December 31, 2007 and 2006. The credit enhancement reserves resulted from swap transactions where the former RTC received mortgage-backed securities in exchange for single-family mortgage loans. The RTC supplied credit enhancement reserves for the mortgage loans in the form of cash collateral to cover future credit losses over the remaining life of the loans. These reserves may cover future credit losses through 2020.

Receivables From Thrift Resolutions and Other Assets, Net at December 31

Dollars in Thousands

	2007	2006
Receivables from closed thrifts	$ 8,367,078	$ 11,308,460
Allowance for losses	(8,359,347)	(11,299,448)
Receivables from Thrift Resolutions, Net	**7,731**	**9,012**
Other assets	27,081	27,718
Total	**$ 34,812**	**$ 36,730**

4 Contingent Liabilities for:

Litigation Losses

The FRF records an estimated loss for unresolved legal cases to the extent those losses are considered probable and reasonably estimable. As of December 31, 2007 and 2006, respectively, $35.4 million and $279.3 million were recorded as probable losses. Additionally, at December 31, 2007, the FDIC has determined that losses from unresolved legal cases totaling $3 million are reasonably possible.

Additional Contingency

Goodwill Litigation

In *United States v. Winstar Corp.*, 518 U.S. 839 (1996), the Supreme Court held that when it became impossible following the enactment of FIRREA in 1989 for the federal government to perform certain agreements to count goodwill toward regulatory capital, the plaintiffs were entitled to recover damages from the United States. Approximately 19 remaining cases are pending against the United States based on alleged breaches of these agreements.

On July 22, 1998, the Department of Justice's (DOJ's) Office of Legal Counsel (OLC) concluded that the FRF is legally available to satisfy all judgments and settlements in the goodwill litigation involving supervisory action or assistance agreements. OLC determined that nonperformance of these agreements was a contingent liability that was transferred to the FRF on August 9, 1989, upon the dissolution of the FSLIC. On July 23, 1998, the U.S. Treasury determined, based on OLC's opinion, that the FRF is the appropriate source of funds for payments of any such judgments and settlements. The FDIC General Counsel concluded that, as liabilities transferred on August 9, 1989, these contingent liabilities for future nonperformance of prior agreements with respect to supervisory goodwill were transferred to the FRF-FSLIC, which is that portion of the FRF encompassing the obligations of the former FSLIC. The FRF-RTC, which encompasses the obligations of the former RTC and was created upon the termination of the RTC on December 31, 1995, is not available to pay any settlements or judgments arising out of the goodwill litigation.

The goodwill lawsuits are against the United States and as such are defended by the DOJ. On January 3, 2008, the DOJ again informed the FDIC that it is "unable at this time to provide a reasonable estimate of the likely aggregate contingent liability resulting from the *Winstar*-related cases." This uncertainty arises, in part, from the existence of significant unresolved issues pending at the appellate or trial court level, as well as the unique circumstances of each case.

The FDIC believes that it is probable that additional amounts, possibly substantial, may be paid from the FRF-FSLIC as a result of judgments and settlements in the goodwill litigation. Based on representations from the DOJ, the FDIC is unable to estimate a range of loss to the FRF-FSLIC from the goodwill litigation. However, the FRF can draw from an appropriation provided by Section 110 of the Department of Justice Appropriations Act, 2000 (Public Law 106-113, Appendix A, Title I, 113 Stat. 1501A-3, 1501A-20) such sums as may be necessary for the payment of judgments and compromise settlements in the goodwill litigation. This appropriation is to remain available until expended. Because an appropriation is available to pay such judgments and settlements, any liability for goodwill litigation should have a corresponding receivable from the U.S. Treasury and therefore have no net impact on the financial condition of the FRF-FSLIC.

The FRF paid $405.1 million as a result of judgments and settlements in six goodwill cases for the year ended December 31, 2007, compared to $194.7 million for four goodwill cases for the year ended December 31, 2006. As described above, the FRF received appropriations from the U.S. Treasury to fund these payments. At December 31, 2007, the FRF accrued a $35.4 million contingent liability and offsetting receivable from the U.S. Treasury for judgments in two additional cases that were fully adjudicated as of year end. These funds *were paid* in January 2008.

In addition, the FRF-FSLIC pays the goodwill litigation expenses incurred by DOJ based on a Memorandum of Understanding (MOU) dated October 2, 1998, between the FDIC and DOJ. Under the terms of the MOU, the FRF-FSLIC paid $11.4 million and $17.5 million to DOJ for fiscal years (FY) 2008 and 2007, respectively. As in prior years, DOJ carried over and applied all unused funds toward current FY charges. At September 30, 2007, DOJ had an additional $5.6 million in unused FY 2007 funds that were applied against FY 2008 charges of $17 million.

Guarini Litigation

Paralleling the goodwill cases are similar cases alleging that the government breached agreements regarding tax benefits associated with certain FSLIC-assisted acquisitions. These agreements allegedly contained the promise of tax deductions for losses incurred on the sale of certain thrift assets purchased by plaintiffs from the FSLIC, even though the FSLIC provided the plaintiffs with tax-exempt reimbursement. A provision in the Omnibus Budget Reconciliation Act of 1993 (popularly referred to as the "Guarini legislation") eliminated the tax deductions for these losses.

Eight Guarini cases were originally filed seeking damages relating to the government's elimination of certain tax deductions. The last of these eight cases concluded in 2007 with a settlement of $23 million being paid. In a case settled in 2006, the settlement agreement further obligates the FRF-FSLIC as a guarantor for all tax liabilities in the event the settlement amount is determined by tax authorities to be taxable. The maximum potential exposure under this guarantee through 2009 is approximately $81 million. After reviewing relevant case law in relation to the nature of the settlement, the FDIC believes that it is very unlikely the settlement will be subject to taxation. Therefore, the FRF is not expected to fund any payment under this guarantee and no liability has been recorded.

Representations and Warranties

As part of the RTC's efforts to maximize the return from the sale of assets from thrift resolutions, representations and warranties, and guarantees were offered on certain loan sales. The majority of loans subject to these agreements have been paid off, refinanced, or the period for filing claims has expired. The FDIC's estimate of maximum potential exposure to the FRF is $18.7 million. No claims in connection with representations and warranties have been asserted since 1998 on the remaining open agreements. Because of the age of the remaining portfolio and lack of claim activity, the FDIC does not expect new claims to be asserted in the future. Consequently, the financial statements at December 31, 2007 and 2006 do not include a liability for these agreements.

5 Resolution Equity

As stated in the Legislative History section of Note 1, the FRF is comprised of two distinct pools: the FRF-FSLIC and the FRF-RTC. The FRF-FSLIC consists of the assets and liabilities of the former FSLIC. The FRF-RTC consists of the assets and liabilities of the former RTC. Pursuant to legal restrictions, the two pools are maintained separately and the assets of one pool are not available to satisfy obligations of the other.

The following table shows the contributed capital, accumulated deficit, and resulting resolution equity for each pool.

Resolution Equity at December 31, 2007

Dollars in Thousands

	FRF-FSLIC	FRF-RTC	FRF Consolidated
Contributed capital - beginning	$ 45,254,659	$ 82,199,337	$ 127,453,996
Add: U.S. Treasury payments/receivable for goodwill litigation	188,586	0	188,586
Less: REFCORP payments	0	(225,000)	(225,000)
Contributed capital - ending	**45,443,245**	**81,974,337**	**127,417,582**
Accumulated deficit	(42,185,100)	(81,584,813)	(123,769,913)
Total	**$ 3,258,145**	**$ 389,524**	**$ 3,647,669**

Contributed Capital

The FRF-FSLIC and the former RTC received $43.5 billion and $60.1 billion from the U.S. Treasury, respectively, to fund losses from thrift resolutions prior to July 1, 1995. Additionally, the FRF-FSLIC issued $670 million in capital certificates to the Financing Corporation (a mixed-ownership government corporation established to function solely as a financing vehicle for the FSLIC) and the RTC issued $31.3 billion of these instruments to the REFCORP. FIRREA prohibited the payment of dividends on any of these capital certificates. Through December 31, 2007, the FRF-RTC has returned $4.556 billion to the U.S. Treasury and made payments of $4.797 billion to the REFCORP. Subsequent to year-end, FRF-RTC paid an additional $225 million to the REFCORP on January 10, 2008. These actions serve to reduce contributed capital.

FRF-FSLIC received $405.1 million in U.S. Treasury payments for goodwill litigation in 2007. Furthermore, $35.4 million and $251.8 million were accrued for as receivables at year-end 2007 and 2006, respectively. The effect of this activity was an increase in contributed capital of $188.6 million in 2007.

Accumulated Deficit

The accumulated deficit represents the cumulative excess of expenses over revenue for activity related to the FRF-FSLIC and the FRF-RTC. Approximately $29.8 billion and $87.9 billion were brought forward from the former FSLIC and the former RTC on August 9, 1989, and January 1, 1996, respectively. The FRF-FSLIC accumulated deficit has increased by $12.4 billion, whereas the FRF-RTC accumulated deficit has decreased by $6.3 billion, since their dissolution dates.

6 Employee Benefits

Pension Benefits

Eligible FDIC employees (permanent and term employees with appointments exceeding one year) are covered by the federal government retirement plans, either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Although the FRF contributes a portion of pension benefits for eligible employees, it does not account for the assets of either retirement system. The FRF also does not have actuarial data for accumulated plan benefits or the unfunded liability relative to eligible employees. These amounts are reported on and accounted for by the U.S. Office of Personnel Management. The FRF's pension-related expenses were $252 thousand and $850 thousand for 2007 and 2006, respectively.

Postretirement Benefits Other Than Pensions

The FRF no longer records a liability for the postretirement benefits of life and dental insurance (a long-term liability), due to the expected dissolution of the FRF. The liability is recorded by the DIF. However, the FRF does continue to pay its proportionate share of the yearly claim expenses associated with these benefits.

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To the Board of Directors
The Federal Deposit Insurance Corporation

In accordance with Section 17 of the Federal Deposit Insurance Act, as amended, we are responsible for conducting audits of the financial statements of the two funds administered by the Federal Deposit Insurance Corporation (FDIC). In our audits of the Deposit Insurance Fund's (DIF) and the FSLIC Resolution Fund's (FRF) financial statements for 2007 and 2006, we found

- the financial statements as of and for the years ended December 31, 2007, and 2006, are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles;
- FDIC had effective internal control over financial reporting (including safeguarding assets) and compliance with laws and regulations for each fund; and
- no reportable noncompliance with laws and regulations we tested.

The following sections discuss in more detail (1) these conclusions; (2) our audit objectives, scope, and methodology; and (3) agency comments and our evaluation.

Opinion on DIF's Financial Statements

The financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, DIF's assets, liabilities, and fund balance as of December 31, 2007, and 2006, and its income and fund balance and its cash flows for the years then ended.

As discussed in note 6 to DIF's financial statements, FDIC's insured financial institutions faced increased challenges in 2007. The downturn in housing markets led to asset-quality problems and volatility in financial markets, which hurt banking industry performance and threatened the viability of some institutions that had significant exposure to higher-risk residential mortgages. It is uncertain how long the effects of this downturn will last. In addition to a recorded estimated liability of $124 million as of December 31, 2007, for the anticipated failure of some DIF insured institutions, FDIC has identified additional risk that could result in a further estimated loss to the DIF of $1.7 billion should potentially vulnerable insured institutions ultimately fail. FDIC continues to evaluate the risks to affected institutions in light of evolving economic conditions, but the impact of such risks on the DIF cannot be reasonably estimated at this time. Actual losses, if any, will largely depend on future economic and market conditions and could differ materially from FDIC's estimates.

Opinion on FRF's Financial Statements

The financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, FRF's assets, liabilities, and resolution equity as of December 31, 2007, and 2006, and its income and accumulated deficit and its cash flows for the years then ended.

Opinion on Internal Control

FDIC management maintained, in all material respects, effective internal control over financial reporting (including safeguarding assets) and compliance as of December 31, 2007, that provided reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements for each fund would be prevented or detected on a timely basis. Our opinion is based on criteria established under 31 U.S.C. 3512 (c), (d), commonly known as the Federal Managers' Financial Integrity Act (FMFIA).

We did identify certain control deficiencies during our 2007 audits. However, we do not consider these control deficiencies to be significant deficiencies.[1] We will be reporting separately to FDIC management on these matters.

[1] A significant deficiency is a control deficiency, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected.

Compliance with Laws and Regulations

Our tests for compliance with selected provisions of laws and regulations disclosed no instances of noncompliance that would be reportable under U.S. generally accepted government auditing standards. However, the objective of our audits was not to provide an opinion on overall compliance with laws and regulations. Accordingly, we do not express such an opinion.

Objectives, Scope, and Methodology

FDIC management is responsible for (1) preparing the annual financial statements in conformity with U.S. generally accepted accounting principles; (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of FMFIA are met; and (3) complying with applicable laws and regulations.

We are responsible for obtaining reasonable assurance about whether (1) the financial statements are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, and (2) management maintained effective internal control, the objectives of which are the following:

1. financial reporting–transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in conformity with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition, and
2. compliance with laws and regulations–transactions are executed in accordance with laws and regulations that could have a direct and material effect on the financial statements.

We are also responsible for testing compliance with selected provisions of laws and regulations that could have a direct and material effect on the financial statements.

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- assessed the accounting principles used and significant estimates made by management;
- evaluated the overall presentation of the financial statements;

- obtained an understanding of the entity and its operations, including its internal control related to financial reporting (including safeguarding assets) and compliance with laws and regulations;
- tested relevant internal controls over financial reporting and compliance, and evaluated the design and operating effectiveness of internal control;
- considered FDIC's process for evaluating and reporting on internal control based on criteria established by FMFIA; and
- tested compliance with certain laws and regulations, including selected provisions of the Federal Deposit Insurance Act, as amended, and the Federal Deposit Insurance Reform Act of 2005.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting and compliance. Because of inherent limitations in internal control, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected. We also caution that projecting our evaluation to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate.

We did not test compliance with all laws and regulations applicable to FDIC. We limited our tests of compliance to those laws and regulations that could have a direct and material effect on the financial statements for the year ended December 31, 2007. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our work in accordance with U.S. generally accepted government auditing standards.

FDIC Comments and Our Evaluation

In commenting on a draft of this report, FDIC's Chief Financial Officer (CFO) reported the agency was pleased to receive unqualified opinions on the DIF and FRF financial statements and that GAO did not identify any material weaknesses or significant deficiencies during the 2007 audits. FDIC's CFO also expressed appreciation for GAO's recognition of FDIC's accomplishments during the 2007 audit year. The CFO added that FDIC is dedicated to promoting the highest standard of financial management and that FDIC will work diligently to sustain that focus. Furthermore, the CFO added that continued improvements in operations remain a priority for FDIC.

The complete text of FDIC's comments is reprinted in appendix I.

David M. Walker
Comptroller General
of the United States

February 4, 2008

FDIC
Federal Deposit Insurance Corporation
550 17th Street, NW Washington, DC 20429 9990 Deputy to the Chairman and Chief Financial Officer

February 4, 2008

Mr. David M. Walker
Comptroller General of the United States
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Re: FDIC Management Response on the GAO 2007 Financial Statements Audit Report

Dear Mr. Walker:

Thank you for the opportunity to comment on the U.S. Government Accountability Office's (GAO) draft audit report titled, **Financial Audit: Federal Deposit Insurance Corporation Funds' 2007 and 2006 Financial Statements, GAO-08-416**. The report presents GAO's opinions on the calendar year 2007 and 2006 financial statements of the Deposit Insurance Fund (DIF) and the Federal Savings and Loan Insurance Corporation Resolution Fund (FRF). The report also presents GAO's opinion on the effectiveness of the Federal Deposit Insurance Corporation's (FDIC's) internal control over financial reporting and compliance with laws and regulations for each of the funds as of December 31, 2007, and GAO's evaluation of FDIC's compliance with selected laws and regulations.

We are pleased that FDIC received unqualified opinions on its financial statements for the sixteenth consecutive year and that there were no material weaknesses or significant deficiencies identified during the 2007 audits. The GAO reported that the funds' financial statements were presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles; FDIC had effective internal control over financial reporting and compliance with laws and regulations for each fund; and there was no reportable noncompliance with laws and regulations that were tested.

We appreciate GAO's recognition of our accomplishments during the 2007 audit year. As always, our management team is dedicated to promoting the highest standard of financial management, and we will work diligently to sustain that focus. Continued improvements in operations remain a priority for FDIC.

In addition, I want to recognize the GAO's support throughout the audit and to acknowledge you and the GAO staff for your efforts and dedication in working with FDIC again this year to meet the accelerated reporting deadline for our audited financial statements. We look forward to continuing this productive and successful relationship in the coming year.

If you have any questions or concerns, please do not hesitate to contact me.

Sincerely,

Steven O. App

Steven O. App
Deputy to the Chairman and
Chief Financial Officer

Overview of the Industry

The 8,560 FDIC-insured commercial banks and savings institutions that filed financial results for the first nine months of 2007 reported net income of $100.7 billion, a decline of 10.7 percent compared to the first nine months of 2006. This is the first year-over-year decline in industry earnings in seven years. The decline in earnings was caused by sharply higher expenses for bad loans, weakness in market-sensitive noninterest revenues, and narrower net interest margins. Fewer than half of all institutions – 49.5 percent – reported year-over-year increases in net income, and the percentage of institutions with negative net income for the first nine months of the year rose to 10.2 percent, up from 7.0 percent a year earlier.

The average return on assets (ROA) for the first nine months was 1.11 percent, down from 1.33 percent for the same period of 2006. This is the lowest nine-month industry ROA since 1996. More than 60 percent of insured institutions had lower ROAs in 2007 than in 2006. Insured institutions set aside $37.1 billion in provisions for loan and lease losses during the first nine months of 2007, an increase of $17.2 billion (86.8 percent) compared to the same period in 2006. The industry's total noninterest income increased by only $1.3 billion (0.7 percent), as income from securitization activities fell by $3.6 billion (18.4 percent), and gains on sales of loans declined by $1.8 billion (32.5 percent). Total noninterest expenses were $11.2 billion (4.4 percent) higher, led by a $5.7-billion (5.0-percent) increase in salary and benefit expenses.

One of the positive trends in income and expenses was the $10.3-billion (4.0-percent) year-over-year increase in net interest income. A difficult interest-rate environment characterized by a flat yield curve contributed to a decline in the industry's net interest margin. The average margin fell from 3.43 percent in the first three quarters of 2006 to 3.32 percent for the first three quarters of 2007. However, the industry's interest-earning assets grew by 7.5 percent from the end of September 2006 through the end of September 2007, helping to boost net interest income.

Signs of asset quality deterioration were clearly evident in 2007. For the 12 months ended September 30, total noncurrent loans and leases – those that were 90 days or more past due or in nonaccrual status – increased by $30.4 billion (57.9 percent). Loans secured by real estate properties accounted for 92 percent ($28.0 billion) of the increase in noncurrent loans. Residential mortgage loans accounted for more than half ($15.4 billion) of the increase in noncurrent loans, while noncurrent real estate construction and development loans increased by $8.4 billion (283 percent). Net charge-offs of loans and leases totaled $27.9 billion in the first three quarters of 2007, an increase of $9.3 billion (49.7 percent) over the same period in 2006. Loans to individuals other than credit cards had the largest year-over-year increase, rising by $2.2 billion (53.8 percent). Net charge-offs of loans to commercial and industrial (C&I) borrowers were $1.8 billion (84.6 percent) higher, and net charge-offs of credit card loans increased by $1.5 billion (15.5 percent). Net charge-offs of residential mortgage loans increased by $1.4 billion (137.5 percent). At the end of September 2007, 65 institutions were on the FDIC's "Problem List," up from a 36-year low of 47 "problem" institutions a year earlier.

Asset growth slowed in 2007, but remained strong by historic standards. During the 12 months ended September 30, total assets of insured institutions increased by $954 billion (8.1 percent). Loans and leases accounted for more than half of the increase in total assets, rising by $527 billion (7.4 percent). Loans to C&I borrowers increased by $208.8 billion (17.7 percent), real estate construction and development loans rose by $71.4 billion (13.1 percent), and real estate loans secured by nonfarm nonresidential properties grew by $53.6 billion (6.1 percent).

Growth in deposits did not keep pace with the increase in total assets. In the 12 months ended September 30, total deposits of insured institutions increased by $603.6 billion (8.0 percent). During that period, growth in foreign office deposits (up $336.6 billion, or 30.5 percent) surpassed growth in domestic office deposits (up $267.0 billion, or 4.1 percent). Nondeposit liabilities increased by $246.5 billion (8.4 percent), and equity capital rose by $103.5 billion (8.5 percent). Merger-related goodwill accounted for almost two-thirds (63 percent) of the increase in equity. At the end of September 2007, more than 99 percent of all FDIC-insured institutions met or exceeded the highest regulatory capital standards[4].

[4] For purposes of Prompt Corrective Action, FDIC-insured institutions are generally considered "well capitalized," the highest category, if they have a total risk-based capital ratio of 10.0 percent or greater, a Tier 1 risk-based capital ratio of 6.0 percent or greater, and a leverage ratio of 5.0 percent or greater.