Flagstar Bancorp ★ 2007 Annual Report

2007 ANNUAL REPORT

Flagstar® Bancorp

20 YEARS OF CONVENIENCE YOU CAN COUNT ON

In 2007, we celebrated 20 years of bringing outstanding products and services to our customers. Because of the conveniences we offer, we figure over all those years we've saved our customers lots of things — like time, gas, paper, and much more. In the pages that follow, we chronicle some of our best "saves." At Flagstar, "convenience you can count on" is not just our tagline — it's our way of doing business.

Save ...

Our growing network of banking centers means that more and more, we're on your corner, on your way home from work or where you shop. Now *that's* convenience you can count on.

#1

STAR TREATMENT: CUSTOMER SERVICE

★

According to a recent survey of Flagstar's retail bank customers by the American Customer Satisfaction Index (ACSI), Flagstar tied with the leading benchmark bank in customer satisfaction and scored higher than the four other major U.S. retail banks in the survey.

★

According to a recent survey by Informa Research Services, Flagstar customers are highly satisfied and more likely to recommend Flagstar than customers of all other banks in the survey.

About Us

Flagstar Bancorp (NYSE: FBC), is the holding company for Flagstar Bank, a federally chartered stock savings bank. Since our founding in 1987, we have experienced exceptional growth, and today we are the largest banking institution headquartered in Michigan. We also are one of the nation's leading mortgage lenders.

We serve our customers through our retail banking centers in Michigan, Indiana and Georgia and our Web site at www.flagstar.com. We are a full-service bank, offering depository, lending and investment products to consumers and businesses. We use customer deposits, along with other funding sources, to invest primarily in single-family residential mortgage loans that we originate and purchase nationwide. We sell most of the mortgage loans we originate.

Our products include consumer loans that we originate principally in the three states where we have a banking presence, home loans and home equity lines of credit, which we originate nationally, and commercial real estate loans in 20 states. In 2007, we expanded our menu of services to our business banking customers to include commercial lending and treasury management services. We also provide warehouse lines of credit to retail lending institutions across the country. In addition, we service a large portfolio of mortgage loans for other investors.

COMMUNITY BANK

Flagstar is a community bank with 164 banking centers in Michigan, Indiana and Georgia, and total deposits of $8.2 billion at December 31, 2007.

HOME LENDER

Flagstar is one of the nation's largest single-family residential prime mortgage originators. We lend to homeowners in all 50 states. Between 2002 and 2007, we originated residential mortgage loans totaling more than $206 billion.

MORTGAGE SERVICER

Flagstar collects mortgage payments and services the loans of more than 285,000 homeowners across the nation.


SAVE at your convenience

Flagstar is there to serve you — sunrise to sunset. Why waste your lunch break rushing to the bank? Our drive-ups are open weekdays 7:30 a.m. to 7:30 p.m.

STAR TREATMENT: MYBRANCH FEATURE

★

Check out the new MyBranch feature on flagstar.com that puts your local branch information right at your fingertips.

Banking

In 2007, we continued to make banking more convenient for our customers by opening 13 new banking centers, seven in Michigan and six in Georgia, a market we first entered in 2005. We were attracted to Georgia because of its diverse, vibrant economy and strong growth prospects, and we're pleased with our progress in winning customers and building name recognition. We're committed to investing in Atlanta and its future, which is why we're expanding our banking presence there and why in 2007 we signed on as the official bank of the Atlanta Falcons pro football team.

A major initiative of 2007-08 has been the redesign and launch of flagstar.com, our corporate Web site. It brings our highly competitive deposit products and home lending expertise within the reach of a vast audience of consumers with a few simple clicks of a mouse. Best of all, visitors to the site can open and fund accounts in 10 minutes or less. It's "anywhere, anytime" banking — the ultimate in convenience you can count on.

Our new Web site complements our other customer-focused services such as our free online banking and bill-pay, online statements, telephone banking and mobile access to accounts via wireless.flagstar.com. Of course, online banking comes with an easy-to-use funds transfer feature — a great way to move money between financial institutions in a safe, secure environment without writing and mailing checks. We've even found a solution to those pesky payments to small service providers such as baby-sitters. It's called Pay People, and it allows customers to pay anyone with an e-mail address and a bank account at any domestic financial institution.


Flagstar Bank
Bank OPEN
Drive-Up OPEN
2
SAVE your lunch break

Our in-store branches are the ultimate in convenience. Bank where you shop — even on Sundays — and save gas as an added bonus.

TOP 5 REASONS TO BANK AT FLAGSTAR

1. Real people hours, not bankers' hours
2. Great new Web site
3. The best customer service (verified by three independent surveys)
4. Loyalty Program that offers interest rate bonus
5. Best Rate Guarantee on CDs

We were an early adopter of new ATM technology that allows customers to make deposits without envelopes. Checks deposited in the ATM are imaged and printed on the receipt, while cash is verified with the customer before the deposit is finalized. We are using this technology in all our Georgia ATMs and new ATMs installed throughout our network. For even more convenience, we'll be placing ATMs in select Wal-Mart service stations in Michigan and Indiana starting in 2008.

For years, we have distinguished ourselves from our competitors with our 7:30 a.m. to 7:30 p.m. weekday drive-up hours and our convenient sit-down banking, which allows customers to handle their banking in comfort and privacy. We also have traditionally offered Sunday hours at our in-store branches in Michigan and Indiana. When we entered the Georgia market, we added Sunday lobby and drive-up hours to provide more convenience to our customers, and now we're doing the same at select traditional banking centers in Michigan and Indiana. In early 2008 we opened our first branch in a Wal-Mart in Georgia.

Customers have been enjoying the safety and convenience of our Visa® debit cards for some time, and recently we added a rewards program that makes "swiping" even more attractive. With every swipe of their card, customers earn points toward great free gifts. And soon we'll be extending the rewards program to our new Flagstar credit card — slated for introduction in 2008. It's an added bonus, just for using our cards.

SAVE *gas*

Our new envelope-free ATMs let you deposit your cash or check directly in the machine. That saves the step — and hassle — of filling out an envelope.

STAR TREATMENT: ACCESS ANYWHERE

★

Take advantage of mobile banking at wireless.flagstar.com.

We also reward customers who frequently use our services such as direct deposit and automatic bill-pay. Once they meet certain thresholds for transactions, they qualify for preferred rates and other special benefits. It's called our Loyalty Program, and it rewards customers for doing what they're probably doing anyway — using our products to simplify their lives.

Another way we offer convenience is our Bank at Work program, which lets customers open accounts and do their banking on the job. The program offers lots of extras, including a no-cost appraisal for new mortgage customers and free online banking and bill-pay. Plus, customers can choose the checking account that best meets their needs, with options ranging from free checking to eChecking.

While historically we've been a market leader in traditional savings plans, we understand our customers may want to diversify into investment vehicles such as mutual funds and annuities. That's why we have Investment & Insurance Services at Flagstar Bank. Working with Essex National Securities, we offer everything from stocks and bonds to life insurance and 401(k) rollovers. Our licensed financial consultants can help customers map a strategy for retirement or save with tax-advantaged investments. These consultants are committed to providing personal attention and professional advice — all available at our local banking centers.

SAVE a step


Full Service ATM
• Cash Withdrawal
• Balance Inquiry
Deposit
Please insert your cash.
You can insert up to 30 bill(s) at one time.

Flagstar's Remote Deposit for business customers brings the bank to your office, saving you trips to the bank, courier costs, processing fees and much more.

STAR TREATMENT: TEAMING UP

★

To spread the word about the convenience and value of banking at Flagstar, in 2007 we became the official bank of the Atlanta Falcons, offering Falcons MVP checking, a co-branded Visa® debit card and much more.

Business Banking

In 2007, we ramped up our commercial and business banking by bringing on seasoned commercial bankers to provide a full range of commercial lending and treasury management services to customers in our banking states.

Small- and medium-size businesses can now enjoy the convenience of tailor-made credit facilities and a wide range of treasury management products and services right in their banking centers — delivered by experienced commercial bankers.

Another convenience recently introduced to business customers is Flagstar Remote Deposit. It allows customers to scan deposits or payments on-site at their place of business, in essence bringing the bank to their office. Paper items are instantly converted to images and sent via the Internet to Flagstar for posting. Customers save trips to the bank and get access to their funds faster. It's more efficient because it automatically balances deposits, even catching duplicates. And it's safer because images — not paper — are transferred. Better yet, it's a bank that is open at our customers' convenience, 24 hours a day, seven days a week.

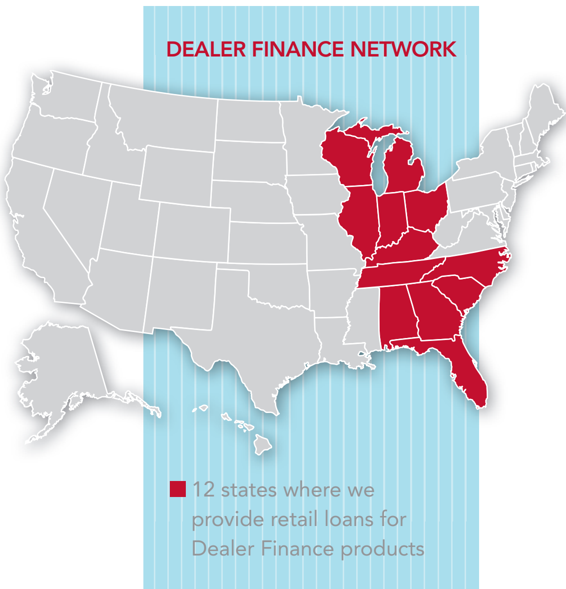
We look for our enhanced business products, coupled with our experienced staff of commercial lenders, to make Flagstar a strong competitor in business banking in the coming years.

Commercial Real Estate Lending

To make it more convenient for our commercial real estate customers to do business with us, we now lend in 20 states, largely in the West, the Midwest and the South. Our transactions range in size from $1 million to $25 million and include office and retail projects, warehouse and industrial properties and multi-family housing. We pride ourselves on our highly competitive interest rates, attractive terms, experienced lenders and knowledgeable, professional staff. Our product line is comprehensive and includes lending, treasury services, investment management to corporations, construction loans, acquisition financing and refinancing and permanent mortgage financing. While we focus primarily on 20 states, we're pleased to look at credit-worthy opportunities around the country.


SAVE a trip
UNISYS

Take advantage of fast approvals — in most cases on the spot — with a Flagstar consumer loan. It's a warp-speed world, so why should approvals be slow?



Retail Home Lending and Direct Lending

We want to make it easy for borrowers to get a home loan, which is why we have so many channels for delivering mortgages. We offer home loans through our network of loan centers across the country, plus additional offices that share space with our banking centers. We also have a toll-free number, (877) 374-3562, where borrowers can talk to home loan advisors in our Direct Lending department. And of course, we offer home loans via our Web site at flagstar.com.

Whether borrowers are buying or refinancing, building or remodeling, we can help them achieve their dreams. With our extensive menu of products, borrowers can choose from hundreds of loan programs. And because we operate nationwide, we can arrange a home loan anywhere in the country. When it comes to home loans, the Flagstar difference is convenience, knowledgeable and professional lenders and fast, friendly service.

Consumer Lending

We've streamlined delivery of our consumer loans by making them available over the phone at (800) 945-7700, online at flagstar.com or at our banking centers. And now we're making it easier for customers to get these loans by providing faster decision-making, in most cases, at the point of sale. We can even print loan documents on the spot.

Traditionally, we have offered home equity lines of credit through our home loan centers. To attract more customers and add convenience, we're now providing these credit lines in our banking centers as well. It's another step toward one-stop shopping. And in 2008, we'll be expanding our product lineup with Flagstar-branded credit cards for consumers and businesses.

Another way we deliver consumer loans is through our dealer finance network. We work with dealers of a variety of consumer products including motorcycles, pianos, pools and spas, power sports equipment and marine and home improvement products to provide loans in 12 states. We also recently opened a marine correspondent program that offers marine loans for a select group of service companies across the country.

We've succeeded by delivering quality service that includes a credit turnaround time of 20 minutes or less on most applications, flexible terms and special programs such as our deferred first-payment feature. To make our dealer financing even more attractive, we offer free electronic funding and free loan set-ups.


SAVE time

We call it our “fuzzy slipper” home loan. With our paperless mortgage, you can “sign” your documents in your kitchen, in your bathrobe — and never touch a scrap of paper.

STAR TREATMENT: AWARD-WINNING TECHNOLOGY

★

Mortgage Technology magazine named us a finalist in its 2007 Technology Awards for our work on eClosings.

Wholesale Lending and Technology Leadership

In 2007, we demonstrated our leadership in mortgage technology by offering customers the option of closing their mortgages electronically. Instead of facing piles of paper, customers who opt for eClosings deal with imaged documents, digital data and eSignatures. It’s all done with the click of a mouse. And instead of leaving the closing with stacks of paper, customers leave with all their documents stored electronically on a flash drive or a CD.

By taking paper out of the system, we reduce courier costs, copying costs and storage costs to our business partners. And that should translate into lower costs for borrowers. Plus, since everything is electronic, documents are easy for borrowers to store, view and retrieve.

Our leadership in paperless processing dates back to 1996 when we first started imaging documents. Now we’ve closed the loop, providing a paperless process from the time documents enter our system, to signatures at closing, all the way through to delivery to investors. Not only are eClosings faster, but they’re also more accurate because the note that’s created is a “smart” document that can be verified electronically.

We’re offering eClosings initially to select borrowers in Michigan, focusing on products we can sell to Fannie Mae. In 2008, we plan to expand to other states and other delivery channels.

We also launched a new company called DocVelocity to bring paperless processing to mortgage originators in our wholesale channel. We call it “paperless in a day,” and it allows originators to go electronic with no special hardware, no special software and no up-front costs. It’s available to all wholesale originators — not just those who sell their loans to Flagstar — for a simple per-loan fee. And because it’s Web-based, it’s easy to use.

Here’s how it works: Originators upload, scan, e-mail or fax their documents to Flagstar where they are automatically imaged, organized and stored digitally. DocVelocity then creates a secure electronic file that can be accessed via the Internet 24/7. Borrowers can even enter their own documents, such as their W-2, into the system on a secure, one-way basis. For originators, it means the opportunity to save money on printing, faxing, copying, delivering and storing documents. To learn more about DocVelocity, call (877) 362-8356 or visit www.docvelocity.com.


SAVE paper

We're on your corner, we're in your corner — involved in your community. And where there's a need, we work with you to save the day. Together, we make our communities better places.

Community

In 2007, Flagstar stepped up its community involvement by hosting more than 130 grassroots events in our banking markets of Michigan, Indiana and Georgia. From the Taste of Clarkston (Michigan) to the Taste of Alpharetta (Georgia), we were involved and invested in our communities.

In our second year of partnering with the March of Dimes, we sponsored 30 charity walks in our three banking states and won the Distinguished March of Dimes Event Support award.

In Michigan, we marked our 10th year as a major sponsor of two premier events in metro Detroit: the *Detroit Free Press*/Flagstar Marathon and Arts, Beats & Eats. We also continued our tradition of sponsoring the Woodward Avenue Dream Cruise, as well as other cruises in metro Detroit. And for the first time, we sponsored a minor league baseball team — the Indianapolis Indians.

As part of our commitment to our communities, we place a special emphasis on volunteerism. That's why we ask all our officers and banking center employees to participate in organizations, events and programs in their communities. In 2007, 865 officers and associates, including banking center staff, volunteered more than 12,000 hours in community service or community reinvestment activities.

In 2007 Flagstar employees once again demonstrated their generosity by holding fundraising events for numerous charities, including the United Way, Make-A-Wish Foundation, Share A Smile, Lighthouse of Oakland County (Michigan) and many others.

In Georgia, 2007 marked the first year of our three-year sponsorship of the Atlanta Falcons football team. As part of the sponsorship, we became the official bank of the team and received exclusive rights to co-branded checking accounts in addition to numerous advertising opportunities to help us build our brand identity in the state.

We also sponsored, supported or were involved in activities relating to our responsibilities under the Community Reinvestment Act. (See sidebar at left.)

In 2008, we look forward to another successful year of sponsorships, grassroots events, volunteerism and commitment to our communities.

COMMUNITY INVESTMENT

MICHIGAN

Community Development Advocates of Detroit
Creekside CDC
Detroit Executive Service Corps
Don Bosco Hall
Grandmont/Rosedale Development Corporation
Habitat for Humanity
Jefferson East Business Assoc.
Kentwood School District
Mission of Peace
Operation Hope, Inc.
Pontiac School District
Warren/Conner Development Coalition

INDIANA

Habitat for Humanity
Indiana Association for Community Economic Development
Indiana Coalition on Housing and Homeless Issues
Indiana Statewide Housing & CED Conference
Indianapolis Neighborhood Housing Partnership
Lutheran Social Services of Indiana
Rebuilding Together

GEORGIA

Accion USA Georgia Program
Habitat for Humanity
HomeStretch
Operation Hope, Inc.
Tallatoona Community Action Partnership

SAVE the day

Flagstar Bank 1987–2007

1987 First Security Savings Bank, now Flagstar Bank, received its charter and opened its first banking center at 1760 Telegraph Rd. in Bloomfield Hills, Mich.

1988 Security Savings assets stood at $270 million, 50 years after opening.

1989

1990 First Security moved to 2600 Telegraph, Bloomfield Hills, Mich.

1991

1992 Expanded home lending operations nationally.

1993 Formed bank holding company.

1994 First Security acquired Security Savings of Jackson, Mich., with offices in Jackson, Eaton Rapids, Parma, Napoleon and Hillsdale.

1995 Assets exceeded $1 billion.

1996 Changed name to Flagstar.

THE EARLY YEARS
SECURITY SAVINGS

1938
Security Savings & Loan Association opened in Jackson, Mich.

1946 – 1955
Assets of Security grew from $6.5 million to $17 million.

1955
Security moved from Otsego at Francis St. to new headquarters at 115 W. Michigan Ave.

1956 – 1975
Assets increased from $18.5 million to $71 million.

1986
Security opened new headquarters at 301 W. Michigan Ave. Security Savings & Loan became Security Savings Bank, a federal savings bank.

FLAGSTAR'S ORIGINS

1968
Thomas Hammond founded his first mortgage company, a predecessor to Flagstar.

1997 — Held Initial Public Offering with a listing on Nasdaq stock exchange.

1998

1999

2000 — Entered agreement to open branches in select Wal-Mart stores.

Entered Indiana banking market.

Opened first in-store banking center at Wal-Mart in Indianapolis.

Moved to new headquarters in Troy, Mich.

2001 — Moved stock listing to New York Stock Exchange.

2002

2003 — Assets exceeded $10 billion.

2004 — Opened 100th banking center.

2005 — Entered Georgia banking market with banking branch in Powder Springs.

Assets exceeded $15 billion.

2006

2007 — Opened 164th banking center.

We have 164 banking centers in three states, 143 home loan offices in 27 states, wholesale offices in 13 states and the ability to write mortgages in all 50 states.

Banking Center Locations

MICHIGAN (117 TOTAL)

Alpena
Ann Arbor (5)
Battle Creek
Big Rapids
Brooklyn
Caledonia
Caro
Charlotte
Coldwater (2)
Commerce Township
Comstock Park
Fenton
Grand Blanc
Grand Haven
Grand Ledge
Grand Rapids (7)
Grandville
Hillsdale
Holland (4)
Jackson (8)
Kalamazoo (3)
Lansing (4)
Ludington
Monroe
Muskegon
New Hudson
Okemos
Saginaw
South Haven
St. Joseph
Sturgis
Three Rivers

GREATER DETROIT AREA (59)

Allen Park
Belleville
Berkley
Beverly Hills
Birmingham
Bloomfield Hills
Brighton
Brownstown Township
Canton (3)
Chesterfield Township (2)
Clarkston
Clinton Township (2)
Dearborn
Dearborn Heights
Detroit (2)
Eastpointe
Farmington Hills (3)
Grosse Pointe (2)
Harrison Township
Howell
Livonia
Macomb Township
Madison Heights (2)
Milford
Novi
Oxford
Pontiac
Rochester (2)
Roseville
Shelby Township (2)
Southgate
Sterling Heights (4)
Taylor (2)
Troy (4)
Warren (2)
Waterford (2)
West Bloomfield (2)
Westland

INDIANA (28 TOTAL)

Angola
Avon
Carmel
Fishers (3)
Fort Wayne (2)
Greenfield
Indianapolis (12)
Kokomo
Lawrence
Muncie
Plainfield
Richmond
Warsaw
Zionsville

GEORGIA (19 TOTAL)

Acworth
Alpharetta
Atlanta
Duluth (2)
Dunwoody (2)
Hiram
Kennesaw
Lawrenceville
Lilburn
Marietta (3)
Powder Springs
Roswell
Smyrna
Snellville
Suwanee

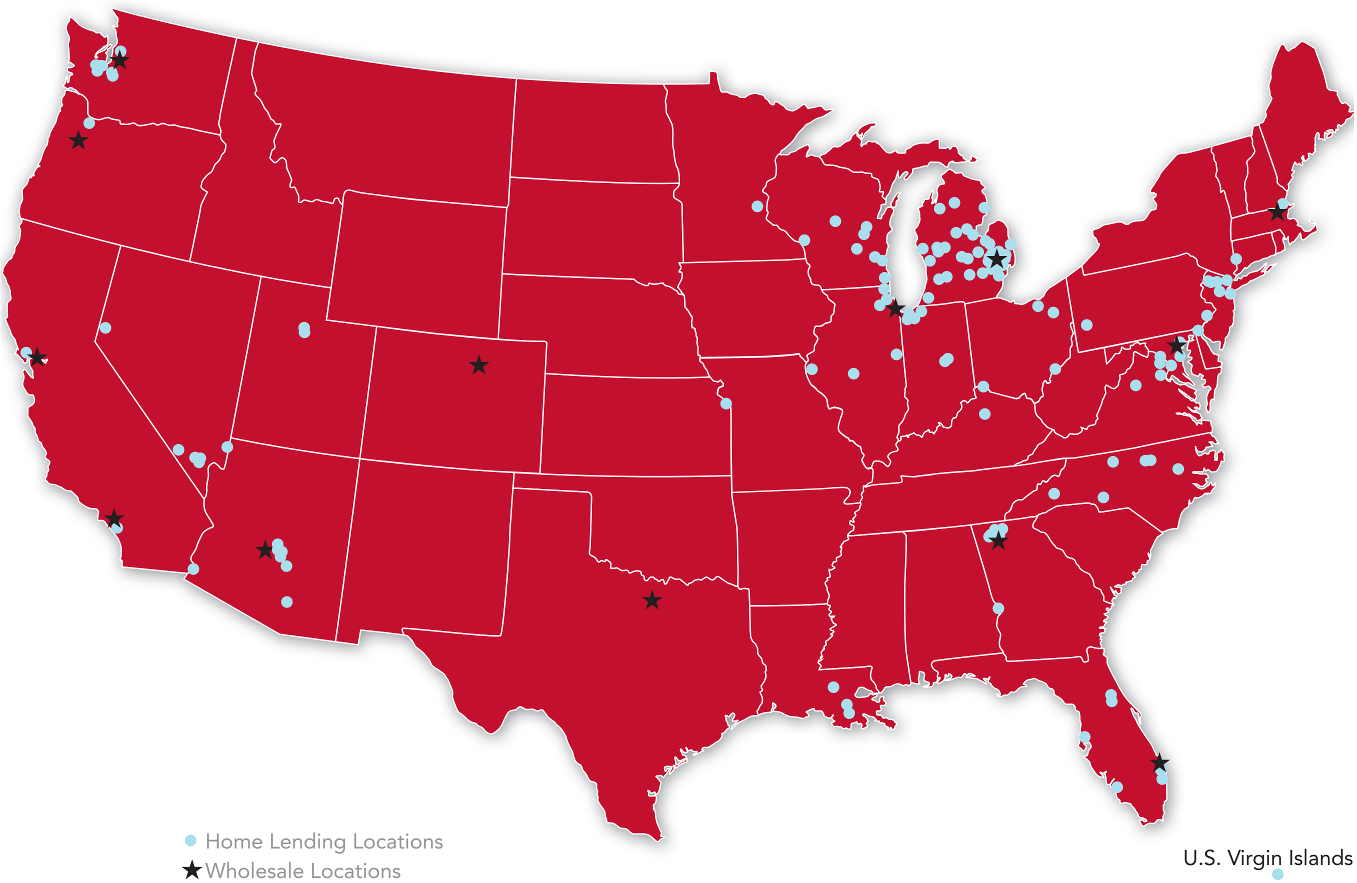
COMING EARLY 2008

Alpharetta, Ga.
Rochester Hills, Mich.
Pontiac, Mich.
St. Clair Shores, Mich.
Indianapolis, Ind.

As of December 31, 2007

From locations across the country, we serve customers in all 50 states.

Home Loan Centers & Wholesale Locations



As of December 31, 2007
Locations are approximate

Letter to Stockholders

MARK T. HAMMOND
President,
Chief Executive Officer

THOMAS J. HAMMOND
Chairman of the Board

In 2007, we continued to execute on our long-term business plan and scored some notable achievements. However, the positives we experienced were overshadowed by market-related challenges such as turmoil in the capital markets, an unfavorable yield curve, worsening credit trends and real estate depreciation in many parts of the country. These market forces played a significant role in our loss for the year.

As a federal savings bank, home lending is a major part of our business. Thus, we were particularly hard hit by rising delinquencies and subsequent charge-offs in home loans, resulting in higher credit costs and the write-down of securities and residuals. We responded proactively to these trends by further tightening credit standards and adding significantly to our collection, loss mitigation and workout staffs. We remain committed to the home lending business and look to position ourselves to take advantage of lucrative market opportunities that will arise as the mortgage industry rebounds.

Despite a disappointing year, we are encouraged by some positives on the horizon. Our banking operations continue to grow, and we recently added new products and staff to help attract business customers. We rolled out our new corporate Web site early in 2008, enhancing our ability to take deposits in all 50 states. Additionally, the prospects for home lending are encouraging. Production in 2007 climbed to $26.7 billion, an increase of 32 percent compared to 2006, and our recent lock volume suggests higher total originations in 2008.

We also roughly doubled our national market share during 2007, following declines in 2005 and 2006, as we avoided originating many types of loans that led to credit losses in the global marketplace in 2007. Minimizing our exposure to subprime loan originations cost us market share and dampened our earnings in the last few years, but we believe the events of the last 12 months have validated our decision.

The turmoil of 2007 has reinforced the value of our deposit franchise and our bank charter, with our banking centers continuing to provide a stable source of deposits. In 2007, we opened 13 new banking centers, seven in Michigan and six in Georgia. In 2008, we plan to hold banking center expansion at about the same level as 2007, with most of our new offices slated for Georgia. We project a growth in retail deposits of 4 to 6 percent, largely coming from our newer banking centers.

As the home lending industry consolidates, we are not only gaining market share but we're also hiring dozens of seasoned, commissioned loan executives to help us grow our business. In addition, we are benefiting from our strong, historical relationships with the FHA and government-sponsored enterprises such as Fannie Mae and Freddie Mac, as the vast majority of our residential mortgages are currently sold in pools guaranteed by those entities.

We believe that Congress' recent action to pass legislation raising the loan limits of Fannie Mae, Freddie Mac and the FHA will position us well to capitalize on new market opportunities. Additionally, we are encouraged by recent improvements in our bank net interest margin, thanks to a lower cost of funds and to increasing spreads between our funding costs and the yields on our assets.

We do not rely on Wall Street for funding, and when the liquidity crisis hit in August 2007, we were prepared with multiple funding sources. These included a growing retail deposit base of $5.1 billion at December 31, 2007, a vibrant public funds division, access to wholesale deposits, a $7.5 billion line of credit with the Federal Home Loan Bank, an unused line of credit with the Federal Reserve discount window and borrowing capacity in the form of federal funds. These funding sources are in addition to a portfolio of agency and AAA-rated mortgage-backed securities that are used as collateral for repo financing through Wall Street when it is cost effective and the capital markets are functioning normally. We remain committed to growing our deposit base and maintaining multiple liquidity sources.

We expect asset balances, including our commercial real estate loans, to remain relatively flat in 2008. However, we do look for an upswing in residential loan originations and sales. We are projecting loan production between $33 and $38 billion in 2008, versus $26.7 billion for 2007, and loan sales between $31 and $36 billion in 2008 versus $24.3 billion for 2007.

As more competitors exit the home lending industry and pricing continues to rationalize, we anticipate higher gains and widening spreads on the sale of our loans.

We have always stated that we manage for the long-term, and we have no intention of changing course now. We have a seasoned management team that has successfully navigated through difficult economic cycles in the past. We will be drawing on this wellspring of experience to help us weather the current challenges. Meanwhile, we are heartened by a number of recognitions we have received in the past year:

- ★ In the fourth quarter 2007, Flagstar engaged the American Customer Satisfaction Index (ACSI) in a research project to compare its customer satisfaction performance to that of five major U.S. retail banks — Bank of America, JP Morgan Chase & Co., Citibank, Wachovia and Wells Fargo & Co. Flagstar tied with Wachovia, the industry leader, and scored significantly higher than the retail bank industry average.

- ★ In a recent survey by Informa Research Services, we ranked No. 1 in overall customer satisfaction. The survey included a broad base of customers of Flagstar and nine major banks, as well as credit unions.

- ★ In a survey conducted by GfK Custom Research North America in the fall of 2006, Flagstar scored significantly higher than the metro Detroit market customer satisfaction benchmark, with eight in 10 customers being highly satisfied with the bank.

- ★ For the fourth consecutive year, *Mortgage Technology* magazine cited us as one of the Top 25 Tech-Savvy Lenders, describing us as a "pioneer in creating a paperless back office." *Mortgage Technology* also named us a 2007 Technology Awards finalist for our work on eClosings.

- ★ For the sixth consecutive year, the Michigan Business and Professional Association recognized us as one of Metro Detroit's 101 Best and Brightest Companies to Work For.

- ★ Freddie Mac named us a Tier One Platinum level servicer for the third consecutive year, recognizing us for superior investor accounting and reporting and default management. We also remain on Standard & Poors Select Servicer list.

Going forward, we reaffirm our commitment to executing our business plan that focuses on long-term profitability, superior customer service and ever-increasing stockholder value. We thank our stockholders for the confidence they have placed in us, and our board members and associates for their dedication to our company.

March 12, 2008

Directors and Management Team

Directors ★ FLAGSTAR BANCORP, INC.

Thomas J. Hammond	Chairman of the Board
Mark T. Hammond	Vice Chairman of the Board, Chief Executive Officer, President
Kirstin A. Hammond	Director, Executive Director
Robert O. Rondeau, Jr.	Director, Executive Director
Charles Bazzy	Director (outside)
James D. Coleman	Director (outside)
Frank D'Angelo	Director (outside)
Robert W. DeWitt	Director (outside)
Richard S. Elsea	Director (outside)
Jay J. Hansen	Director (outside)
Michael Lucci, Sr.	Director (outside)
William F. Pickard	Director (outside)
Brian Tauber	Director (outside)

Management Team ★ FLAGSTAR BANK, FSB

Thomas J. Hammond	Chairman of the Board
Mark T. Hammond	Chief Executive Officer, President
Kirstin A. Hammond	Executive Director, Chief Investment Officer
Robert O. Rondeau, Jr.	Executive Director, Commercial and Consumer Lending
Joan H. Anderson	Executive Vice President, Loan Administration
Paul D. Borja	Executive Vice President, Chief Financial Officer
M. David Bowers	Executive Vice President, Wholesale Lending
W. Steven Brooks	Executive Vice President, Chief Operating Officer, Lending
Alessandro P. DiNello	Executive Vice President, Banking
Charles C. Kirkpatrick	Executive Vice President, Chief Technology Officer
Rebecca A. Lucci	Executive Vice President, Human Resources
William M. Robinson III	Executive Vice President, Home Lending
Matthew I. Roslin	Executive Vice President, Chief Legal Officer
Mary Kay Ruedisueli	Executive Vice President, Administration
Craig A. Burres	Senior Vice President, Chief Audit Officer
Steven M. Laidlaw	Senior Vice President, Chief Risk Officer

SHAREHOLDER ASSISTANCE

For help with name, address or stock ownership changes, to report lost or stolen stock certificates or to get assistance with other shareholder issues, please contact our agent directly:

Registrar and Transfer Company
Attention: Investor Relations
10 Commerce Drive
Cranford, NJ 07016
(800) 368-5948
e-mail: info@rtco.com
www.rtco.com

EQUAL HOUSING LENDER Member FDIC FBC LISTED NYSE

In all communication with Registrar and Transfer Company, be sure to mention Flagstar Bancorp and provide your name as it appears on your stock certificate, along with your Social Security number, daytime phone number and current address. In addition, individual investors may report a change of address, request a shareholder account transcript, place a stop on a certificate or obtain a variety of forms by logging on to www.rtco.com and clicking Investor Services.

DIVIDEND REINVESTMENT PLAN

Under Flagstar Bancorp's dividend reinvestment plan, registered stockholders may purchase additional shares of Flagstar Bancorp stock by reinvesting their cash dividends. There is no minimum investment required to participate in the plan. For more information, contact Registrar and Transfer Company.

DIRECT DEPOSIT OF DIVIDENDS

Registered stockholders of Flagstar Bancorp common stock may have their dividend payments deposited into their checking, savings or money market account at any financial institution in the U.S. that accepts electronic deposits. A brochure describing the service and an authorization form are available from the Registrar and Transfer Company.

EQUAL EMPLOYMENT OPPORTUNITY

Flagstar Bancorp does not discriminate against any person on the basis of race, color, religion, national origin, sex, age, handicap, height, weight, familial status, sexual orientation, marital status, veteran disability, Vietnam veteran or other protected veteran or recently separated veteran with respect to recruiting, hiring, promoting, transferring, terminating and other terms and conditions of employment.

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

FORM 10-K

(Mark One)

☑ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2007

OR

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

Commission File Number: **001-16577**

Flagstar® Bancorp, Inc.

(Exact name of registrant as specified in its charter)

Michigan	38-3150651
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5151 Corporate Drive, Troy, Michigan	**48098-2639**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: **(248) 312-2000**

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

Title of each class	Name of each exchange on which registered
Common Stock, par value $0.01 per share	**New York Stock Exchange**

Securities registered pursuant to Section 12(g) of the Act: **None**

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

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

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

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

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

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

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

The estimated aggregate market value of the voting common stock held by non-affiliates of the registrant, computed by reference to the closing sale price ($12.05 per share) as reported on the New York Stock Exchange on June 29, 2007, was approximately $507.3 million. The registrant does not have any non-voting common equity shares.

As of March 11, 2008, 60,325,344 shares of the registrant's Common Stock, $0.01 par value, were issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement relating to its 2008 Annual Meeting of Stockholders have been incorporated into Part III of this Report on Form 10-K.

Table of Contents

Cautions Regarding Forward-Looking Statements

This report contains certain forward-looking statements with respect to the financial condition, results of operations, plans, objectives, future performance and business of Flagstar Bancorp, Inc. ("Flagstar" or the "Company") and these statements are subject to risk and uncertainty. Forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995, include those using words or phrases such as "believes," "expects," "anticipates," "plans," "trend," "objective," "continue," "remain," "pattern" or similar expressions or future or conditional verbs such as "will," "would," "should," "could," "might," "can," "may" or similar expressions. There are a number of important factors that could cause our future results to differ materially from historical performance and these forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed under the heading "Risk Factors" in Part I, Item 1A of this Form 10-K. The Company does not undertake, and specifically disclaims any obligation, to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

PART I

ITEM 1. BUSINESS

Where we say "we," "us," or "our," we usually mean Flagstar Bancorp, Inc. In some cases, a reference to "we," "us," or "our" will include our wholly-owned subsidiary Flagstar Bank, FSB, and Flagstar Capital Markets Corporation ("FCMC"), its wholly-owned subsidiary, which we collectively refer to as the "Bank."

General

The Company is a Michigan-based savings and loan holding company founded in 1993. Our business is primarily conducted through our principal subsidiary, Flagstar Bank, FSB (the "Bank"), a federally chartered stock savings bank. At December 31, 2007, our total assets were $15.8 billion, making us the largest publicly held savings bank in the Midwest and one of the top 15 largest savings banks in the United States.

The Bank is a member of the Federal Home Loan Bank of Indianapolis ("FHLB") and is subject to regulation, examination and supervision by the Office of Thrift Supervision ("OTS") and the Federal Deposit Insurance Corporation ("FDIC"). The Bank's deposits are insured by the FDIC through the Deposit Insurance Fund ("DIF").

At December 31, 2007, we operated 164 banking centers (of which 42 are located in retail stores such as Wal-Mart) located in Michigan, Indiana and Georgia. We also operate 143 home loan centers located in 27 states. This includes an additional 13 banking centers we opened during 2007, including six in Georgia. Our plan over the next five years is to increase our earning asset base and banking center network. To do this, we plan to continue to add banking centers and grow our lending channels in an effort to expand our market share in the markets we serve and to penetrate new markets. Toward this goal, during 2008, we expect to expand our banking center network by up to 13 new banking centers, with seven in Georgia.

Our earnings include net interest income from our retail banking activities, and non-interest income from sales of residential mortgage loans to the secondary market, the servicing of loans for others, the sale of servicing rights related to mortgage loans serviced and fee-based services provided to our customers. Approximately 97.4% of our total loan production during 2007 represented mortgage loans and home equity lines of credit that were collateralized by first or second mortgages on single-family residences.

At December 31, 2007, we had 3,960 full-time equivalent salaried employees of which 877 are account executives and loan officers.

Operating Segments

Our business is comprised of two operating segments — banking and home lending. Our banking operation offers a line of consumer and commercial financial products and services to individuals and to small and middle market businesses through a network of banking centers (i.e., our bank branches) in Michigan, Indiana, and Georgia. Our home lending operation originates, acquires, sells and services mortgage loans on one-to-four family residences. Each operating segment supports and complements the operations of the other, with funding for the home lending operation primarily provided by deposits and borrowings obtained through the banking operation. Financial information regarding our two operating segments is set forth in Note 26 to our consolidated financial statements included in this report under "Item 8. Financial Statements and Supplementary Data." A more detailed discussion of our two operating segments is set forth below.

Banking Operation. Our banking operation collects deposits and offers a broad base of banking services to consumer, municipal and commercial customers. We collect deposits at our 164 banking centers and via the Internet. We also sell certificates of deposit through independent brokerage firms. In addition to deposits, we borrow funds by obtaining advances from the FHLB or by entering into repurchase agreements using as collateral our mortgage-backed securities that we hold as investments. The banking operation invests these funds in a variety of consumer and commercial loan products.

We have developed a variety of deposit products ranging in maturity from demand-type accounts to certificates with maturities of up to ten years, savings accounts and money market accounts. We primarily rely upon our network of strategically located banking centers, the quality and efficiency of our customer service, and our pricing policies to attract deposits.

In past years, our national accounts division garnered funds through nationwide advertising of deposit rates and the use of investment banking firms ("wholesale deposits"). During 2005, 2006 and through June 2007, we did not solicit any funds through the national accounts division as we had access to more attractive funding sources through FHLB advances, security repurchase agreements and other forms of deposits that had the potential for a long term customer relationship. Beginning in July 2007, wholesale deposits became attractive from a cost of funds standpoint, so we began to solicit funds through this division again.

While our primary investment vehicle is single-family residential first mortgage loans originated or acquired by our home lending operation, our banking operation offers consumer and commercial financial products and services to individuals and to small to middle market businesses. During the past three years, we have placed increasing emphasis on commercial real estate lending and on expanding on our commercial lending as a diversification from our national mortgage lending platform. In 2006, we expanded our commercial real estate lending to add 19 states to diversify our lending activity beyond Michigan, Indiana and Georgia.

During 2007, we originated a total of $742.2 million in consumer loans versus $1.1 billion originated in 2006. At December 31, 2007, our consumer loan portfolio totaled $338.2 million or 4.1% of our investment loan portfolio, and contained $56.5 million of second mortgage loans, $179.8 million of home equity lines of credit, and $101.9 million of various other consumer loans.

We also offer a full line of commercial loan products and banking services especially developed for our commercial customers. Commercial loans are made on a secured or unsecured basis, but a vast majority are also collateralized by personal guarantees of the principals of the borrowing business. Assets providing collateral for secured commercial loans require an appraised value sufficient to satisfy our loan-to-value ratio requirements. We also generally require that our commercial customers maintain a minimum debt-service coverage ratio. In addition, we consider the creditworthiness and managerial ability of our borrowers, the enforceability and collectibility of any relevant guarantees and the quality of the collateral.

At December 31, 2007, our commercial real estate loan portfolio totaled $1.5 billion, or 19.2% of our investment loan portfolio, and our non-real estate commercial loan portfolio was $23.0 million, or 0.3% of our investment loan portfolio. At December 31, 2006, our commercial real estate loan portfolio totaled $1.3 billion or 14.6% of our investment loan portfolio, and our non-real estate commercial loan portfolio totaled $14.6 million, or 0.2% of our investment loan portfolio. During 2007, we originated $639.9 million of commercial loans versus $671.5 million in 2006.

We also offer warehouse lines of credit to other mortgage lenders. These lines allow the lender to fund the closing of a mortgage loan. Each extension or drawdown on the line is collateralized by the mortgage loan being funded, and in many cases, we subsequently acquire the mortgage loan. These lines of credit are, in most cases, personally guaranteed by a qualified principal officer of the borrower. The aggregate amount of warehouse lines of credit granted to other mortgage lenders at December 31, 2007, was $1.2 billion, of which $316.7 million was outstanding at December 31, 2007. At December 31, 2006, $1.2 billion in warehouse lines of credit had been granted, of which $291.7 million was outstanding.

Our banking operation also offers a variety of other value-added, fee-based banking services.

Home Lending Operation. Our home lending operation originates, acquires, sells and services single-family residential mortgage loans. The origination or acquisition of residential mortgage loans constitutes our most significant lending activity. At December 31, 2007, approximately 62.7% of our interest-earning assets consisted of first mortgage loans on single-family residences.

During 2007, we were one of the country's leading mortgage loan originators. We utilize three production channels to originate or acquire mortgage loans — Retail, Broker and Correspondent. Each production channel produces similar mortgage loan products and applies, in most instances, the same underwriting standards.

- ***Retail.*** In a retail transaction, we originate the loan through our nationwide network of 143 home loan centers, as well as from our 164 banking centers located in Michigan, Indiana and Georgia and our national call center located in Troy, Michigan. When we originate loans on a retail basis, we complete the origination documentation inclusive of customer disclosure and other aspects of the lending process and fund the transaction internally. During 2007, we closed $2.0 billion of loans utilizing this origination channel, which equaled 7.8% of total originations as compared to $2.1 billion or 11.7% of total originations in 2006 and $4.0 billion or 14.2% of total originations in 2005.

- ***Broker.*** In a broker transaction, an unaffiliated mortgage brokerage company completes the loan paperwork, but we supply the funding for the loan at closing (also known as "table funding") and thereby become the lender of record. At closing, the broker may receive an origination fee from the borrower and we may also pay the broker a fee to acquire the mortgage servicing rights on the loan. We currently have active broker relationships with over 6,200 mortgage brokerage companies located in all 50 states. Brokers remain our largest loan production channel. During 2007, we closed $12.4 billion utilizing this origination channel, which equaled 49.3% of total originations, as compared to $9.0 billion or 48.3% in 2006 and $16.1 billion or 57.1% in 2005.

- ***Correspondent.*** In a correspondent transaction, an unaffiliated mortgage company completes the loan paperwork and also supplies the funding for the loan at closing. We acquire the loan after the mortgage company has funded the transaction, usually paying the mortgage company a market price for the loan plus a fee to acquire the mortgage servicing rights on the loan. Unlike several of our competitors, we do not generally acquire loans in "bulk" from correspondents but rather, we acquire each loan on a loan-level basis and require that each loan be originated to our underwriting guidelines. We have active correspondent relationships with over 1,200 companies located in all 50 states. During 2007, we closed $10.8 billion utilizing this origination channel, which equaled 42.9% of total originations versus $7.2 billion or 40.0% originated in 2006 and $8.1 billion or 28.7% originated in 2005.

We maintain 15 sales support offices that assist our brokers and correspondents nationwide. We also continue to make increasing use of the Internet as a tool to facilitate the mortgage loan origination process through our broker and correspondent production channels. Our brokers and correspondents are able to register and lock loans, check the status of in-process inventory, deliver documents in electronic format, generate closing documents, and request funds through the Internet. Since 2006, virtually all mortgage loans that closed used the Internet in the completion of the mortgage origination or acquisition process. We expect to continue to utilize technology to streamline the mortgage origination process and bring service and convenience to our correspondent partners and customers.

Underwriting. Mortgage loans acquired or originated by the home lending operation are underwritten on a loan-by-loan basis rather than on a pool basis. In general, mortgage loans produced through any of our production channels are reviewed by one of our in-house loan underwriters or by a contract underwriter employed by a mortgage insurance company. However, certain of our correspondents have delegated underwriting authority. Any loan not underwritten by a Flagstar- employed underwriter must be warranted by the underwriter's employer, whether it is a mortgage insurance company or correspondent mortgage company.

We believe that our underwriting process, which relies on the electronic submission of data and images and is based on an imaging workflow process, allows for underwriting at a higher level of accuracy and timeliness than exists with processes that rely on paper submissions. We also provide our underwriters with integrated quality control tools, such as automated valuation models ("AVMs"), multiple fraud detection engines and the ability to electronically submit IRS Form 4506s, to ensure underwriters have the information that they need to make informed decisions. The process begins with the submission of an electronic application and an initial determination of eligibility. The application and required documents are then faxed or uploaded to our corporate underwriting department and all documents are identified by optical character recognition or our underwriting staff. The underwriter is responsible for checking the data integrity and reviewing credit. The file is then reviewed in accordance with the applicable guidelines established by us for the particular product.

Quality control checks are performed by the underwriting department, using the tools outlined above, as necessary, and a decision is then made and communicated to the prospective borrower.

Mortgage Loans. All mortgage loans acquired or originated by our home lending operation are collateralized by a first mortgage on a one-to-four family residential property. A large majority of our mortgage loan products conform to the respective underwriting guidelines established by Fannie Mae, Ginnie Mae or Freddie Mac, which we collectively refer to as the "Agencies". We generally require that any first mortgage loan with a loan-to-value ratio in excess of 80% carry mortgage insurance. A loan-to-value ratio is the percentage that the original principal amount of a loan bears to the appraised value of the mortgaged property at the time of underwriting. However, in the case of a purchase money mortgage loans, in which the loan proceeds are used to acquire the property rather than refinance an existing mortgage loan, we use the lower of the appraised value of the property or the purchase price of the property securing the loan in determining this ratio. We also verify the reasonableness of the appraised value of loans by utilizing an AVM. We generally require a lower loan-to-value ratio, and thus a higher down payment, for loans on homes that are not occupied as a principal residence by the borrower. In addition, all first mortgage loans originated are subject to requirements for title, flood, windstorm, fire, and hazard insurance. Real estate taxes are generally collected and held in escrow for disbursement. We are also protected against fire or casualty loss on home mortgage loans by a blanket mortgage impairment insurance policy that insures us when the mortgagor's insurance is inadequate.

Construction Loans. Our home lending operation also makes short-term loans for the construction of one-to-four family residential housing throughout the United States, with a large concentration in our southern Michigan market area. These construction loans usually convert to permanent financing upon completion of construction. All construction loans are collateralized by a first lien on the property under construction. Loan proceeds are disbursed in increments as construction progresses and as inspections warrant. Construction/permanent loans may have adjustable or fixed interest rates and are underwritten in accordance with the same terms and requirements as permanent mortgages, except that during a construction period, generally up to nine months, the borrower is required to make interest-only monthly payments. Monthly payments of principal and interest commence one month from the date the loan is converted to permanent financing. Borrowers must satisfy all credit requirements that would apply to permanent mortgage loan financing prior to receiving construction financing for the subject property. During 2007, we originated a total of $126.7 million in construction loans versus $114.8 million originated in 2006 and $103.9 million originated in 2005. At December 31, 2007, our portfolio of loans held for investment included $90.4 million of loans secured by properties under construction, or 1.12% of total loans held for investment.

Secondary Market Loan Sales and Securitizations. We sell a majority of the mortgage loans we produce into the secondary market on a whole loan basis or by securitizing the loans into mortgage-backed securities.

The following table indicates the breakdown of our loan sales/securitizations for the period as indicated:

	For the Year Ended December 31,		
	2007 Principal Sold %	2006 Principal Sold %	2005 Principal Sold %
Agency Securitizations	89.74%	83.14%	89.56%
Whole Loan Sales	6.49%	14.57%	7.88%
Private Securitizations	3.77%	2.29%	2.56%
Total	100.00%	100.00%	100.00%

Most of the mortgage loans that we sell are securitized through the Agencies. In an Agency securitization, we exchange mortgage loans that are owned by us for mortgage-backed securities that are guaranteed by Fannie Mae or Freddie Mac or insured through Ginnie Mae and are collateralized by the same mortgage loans that were exchanged. Most or all of these mortgage-backed securities may then be sold to secondary market investors, which may be the Agencies or other third parties in the secondary market. We receive cash payment for these securities upon the settlement dates of the respective sales, at which time we also transfer the related mortgage-backed securities to the purchaser.

We have also securitized a smaller portion of our mortgage loans through a process which we refer to as a private-label securitizations, to differentiate it from an Agency securitization. In a private-label securitization, we sell mortgage loans to our wholly-owned bankruptcy remote special purpose entity, which then sells the mortgage loans to a separate, transaction-specific trust formed for this purpose in exchange for cash and certain interests in the trust and those mortgage loans. Each trust then issues and sells mortgage-backed securities to third party investors that are secured by payments on the mortgage loans. These securities are rated by two of the nationally recognized statistical rating organizations (i.e. — rating agencies.) We have no obligation to provide credit support to either the third-party investors or the trusts, although we are required to make certain servicing advances with respect to mortgage loans in the trusts. Neither the third-party investors nor the trusts generally have recourse to our assets or us, nor do they have the ability to require us to repurchase their mortgage-backed securities. We do not guarantee any mortgage-backed securities issued by the trusts. However, we do make certain customary representations and warranties concerning the mortgage loans as discussed below, and if we are found to have breached a representation or warranty, we could be required to repurchase the mortgage loan from the applicable trust. Each trust represents a "qualifying special purpose entity," as defined under Statement of Financial Accounting Standard ("SFAS") 140, *Accounting for Transfer and Servicing of Financial Assets and Extinguishments of Liabilities, a replacement of FASB Statement No. 125,* and therefore is not consolidated for financial reporting purposes.

In addition to the cash we receive from the securitization of mortgage loans, we retain certain interests in the securitized mortgage loans and the trusts. Such retained interests include residual interests, which arise as a result of our private-label securitizations, and mortgage servicing rights ("MSRs"), which can arise as a result of our Agency securitizations, our private-label securitizations, or both.

The residual interests created upon the issuance of private-label securitizations represent the first loss position and are not typically rated by any nationally recognized statistical rating organization. The value of residual interests represents the present value of the future cash flows expected to be received by us from the excess cash flows created in the securitization transaction. Excess cash flows are dependent upon various factors including estimated prepayment speeds, credit losses and over-collateralization requirements. Residual interests are not typically entitled to any cash flows until both the over-collateralization account, which represents the difference between the bond balance and the value of the collateral underlying the security, has reached a certain level and certain expenses are paid. The over-collateralization requirement may increase if certain events occur, such as increases in delinquency rates or cumulative losses. If certain expenses are not paid or over-collateralization requirements are not met, the trustee applies cash flows to the over-collateralization account until such requirements are met and no excess cash flows would flow to the residual interest. A delay in receipt of, or reduction in the amount of excess cash flows would result in a lower valuation of the residual interests.

Residual interests are designated by us as trading or available-for-sale securities at the time of securitization and are periodically evaluated for impairment. The available-for-sale residual interests are marked to market with changes in the value recognized in other comprehensive income, net of tax. If available-for-sale residual interests are deemed to be impaired and the impairment is considered other-than-temporary, the impairment is recognized in the current period earnings. The trading residual interests are marked to market in the current period earnings. We use an internally developed model to value the residual interest. The model takes into consideration the cash flow structure specific to each transaction, such as over-collateralization requirements and trigger events, and key valuation assumptions, including credit losses, prepayment rates and discount rates.

Upon our sale of mortgage loans, we may retain the servicing of the securitized mortgage loans, or even sell them to other secondary market investors. In general, we do not sell the servicing rights to mortgage loans that we originate for our own portfolio or that we privately securitize. When we retain MSRs, we are entitled to receive a servicing fee equal to a specified percentage of the outstanding principal balance of the loans. We may also be entitled to receive additional servicing compensation, such as late payment fees and earn additional income through the use of non-interest bearing escrows.

When we sell mortgage loans, whether through Agency securitizations, private-label securitizations or on a whole loan basis, we make customary representations and warranties to the purchasers about various characteristics of each loan, such as the manner of origination, the nature and extent of underwriting standards applied and the types of documentation being provided. If a defect in the origination process is identified, we may be required to either repurchase the loan or indemnify the purchaser for losses it sustains on the loan. If there are no such defects, we have no liability to the purchaser for losses it may incur on such loan. We maintain a secondary market reserve to account for the expected losses related to loans we might be required to repurchase (or the indemnity payments we may have to make to purchasers). The secondary market reserve takes into account both our estimate of expected losses on loans sold during the current accounting period as well as adjustments to our previous estimates of expected losses on loans sold. In each case, these estimates are based on our most recent data regarding loan repurchases, actual credit losses on repurchased loans, loss indemnifications and recovery history, among other factors. Increases to the secondary market reserve for current loan sales reduce our net gain on loan sales. Adjustments to our previous estimates are recorded as an increase or decrease in our other fees and charges. The amount of our secondary market reserve equaled $27.6 million and $24.2 million at December 31, 2007 and 2006, respectively.

Loan Servicing. The home lending operation also services mortgage loans for others. Servicing residential mortgage loans for third parties generates fee income and represents a significant business activity for us. During 2007, 2006 and 2005, we serviced portfolios of mortgage loans that averaged $23.4 billion, $20.3 billion and $26.8 billion, respectively. The servicing generated gross revenue of $91.1 million, $82.6 million and $103.3 million in 2007, 2006, and 2005, respectively. This revenue stream was offset by the amortization of $78.3 million, $69.6 million and $94.5 million in previously capitalized values of MSRs in 2007, 2006, and 2005, respectively. When a loan is prepaid or refinanced, any remaining MSR for that loan is fully amortized and therefore amortization expense in a period could exceed loan administration income. During a period of falling or low interest rates, the amount of amortization expense typically increases because of prepayments and refinancing of the underlying mortgage loans. During a period of higher or rising interest rates, payoffs and refinancing typically slow, reducing the rate of amortization.

As part of our business model, we occasionally sell MSRs into the secondary market if we determine that market prices provide us with an opportunity for appropriate profit or for capital management, balance sheet management or interest rate risk purposes. Over the past three years, we sold $40.3 billion of loans serviced for others underlying our MSRs, including $3.6 billion in 2007. The MSRs are sold in transactions separate from the sale of the underlying loans. At the time of the sale, we record a gain or loss based on the selling price of the MSRs less the carrying value and transaction costs. The market price of MSRs changes with demand and the general level of interest rates.

Other Business Activities

We conduct business through a number of wholly-owned subsidiaries in addition to the Bank.

Douglas Insurance Agency, Inc. Douglas Insurance Agency, Inc. (“Douglas”) acts as an agent for life insurance and health and casualty insurance companies. Douglas also acts as a broker with regard to certain insurance product offerings to employees and customers. Douglas’ activities are not material to our business.

Flagstar Reinsurance Company. Flagstar Reinsurance Company (“FRC”) is a wholly-owned subsidiary of the Company that was formed during 2007 as a successor in interest to another wholly-owned subsidiary, Flagstar Credit Inc., a reinsurance company which was subsequently dissolved in 2007. FRC is a reinsurance company that provides credit enhancement with respect to certain pools of mortgage loans underwritten and originated by us during each calendar year. With each pool, all of the primary risk is initially borne by one or more unaffiliated private mortgage insurance companies. A portion of the risk is then ceded to FRC by the insurance company, which remains principally liable for the entire amount of the primary risk. To effect this, the private mortgage insurance company provides loss coverage for all foreclosure losses up to the entire amount of the “insured risk” with respect to each pool of loans. The respective private mortgage insurance company then cedes a portion of that risk to FRC and pays FRC a corresponding portion of the related premium. The mortgage insurance company usually retains the portion of the insured risk ranging from 0% to 5% and from 10.01% to 100% of the insured risk. FRC's share of the total amount of the insured risk is an intermediate tranche of credit enhancement risk which covers the 5.01% to 10% range, and therefore its maximum exposure at any time equals 5% of the insured risk of the insured pools. At December 31, 2007, FRC's maximum exposure amounted to $143.9 million. Pursuant to our individual agreements with the private mortgage insurance companies, we are obligated to maintain cash in a separately managed account for the benefit of these mortgage insurance companies to cover any losses experienced in the portion ceded to us. The amounts we maintain are determined periodically by these companies and reflect their overall assessment at the time of our probability of maximum loss related to our ceded portion and the related severity of such loss. Pursuant to these agreements, we are not obliged to provide any funds to the mortgage insurance companies to cover any losses in our ceded portion other than the funds we are required to maintain in this separately managed account. At December 31, 2007, this separately managed account had a balance of $26.1 million. However, we believe the actual risk of loss is much lower because the credit enhancement is provided on an aggregated pool basis rather than on an individual loan basis. Also, FRC's obligation is subordinated to the primary insurers, and we believe that the insured mortgage loans are fully collateralized. As such, while FRC does bear some risk in the structure, we believe FRC's actual risk exposure is minimal. As of December 31, 2007, no claim had been made against FRC on the mortgage loan credit enhancement it provides.

Flagstar Credit, Inc. Flagstar Credit, Inc. ("FCI"), a wholly-owned subsidiary of the Company, transferred all of its assets to FRC effective October 1, 2007. The transfer was with the approval of each of the mortgage insurers and all actual and contingent liabilities that FCI had at the time were assumed by FRC without any further recourse to FCI and FRC succeeded to all rights and obligations of the agreements with the private mortgage insurers. Following this transfer, FRC has continued the operations of FCI without change and FCI ceased operation and was dissolved in 2007.

Paperless Office Solutions, Inc. Paperless Office Solutions, Inc. ("POS"), a wholly-owned subsidiary of the Company, provides on-line paperless office solutions for mortgage originators. DocVelocity is the flagship product developed by POS to bring web-based paperless mortgage processing to mortgage originators.

Other Flagstar Subsidiaries. In addition to the Bank, Douglas, FRC and POS, we have a number of wholly-owned subsidiaries that are inactive. We also own nine statutory trusts that are not consolidated with our operations. For additional information, see Notes 2 and 15 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplemental Data, herein.

Flagstar Bank. The Bank, our primary subsidiary, is a federally chartered, stock savings bank headquartered in Troy, Michigan. The Bank is also the sole shareholder of FCMC.

Flagstar Capital Markets Corporation. FCMC is a wholly-owned subsidiary of the Bank and its functions include holding investment loans, purchasing securities, selling and securitizing mortgage loans, maintaining and selling mortgage servicing rights, developing new loan products, establishing pricing for mortgage loans to be acquired, providing for lock-in support, and managing interest rate risk associated with these activities.

Flagstar ABS LLC. Flagstar ABS LLC ("ABS") is a wholly-owned subsidiary of FCMC that serves as a bankruptcy remote special purpose entity that has been created to hold trust certificates in connection with our private securitization offerings.

Other Bank Subsidiaries. The Bank, in addition to FCMC, also wholly-owns several other subsidiaries, all of which were inactive at December 31, 2007.

Regulation and Supervision

Both the Company and the Bank are subject to regulation by the OTS. Also, the Bank is a member of the FHLB and its deposits are insured by the FDIC through the DIF. Accordingly, it is subject to an extensive regulatory framework which imposes activity restrictions, minimum capital requirements, lending and deposit restrictions and numerous other requirements primarily intended for the protection of depositors, federal deposit insurance funds and the banking system as a whole, rather than for the protection of shareholders and creditors. Many of these laws and regulations have undergone significant changes in recent years and are likely to change in the future. Future legislative or regulatory change, or changes in enforcement practices or court rulings, may have a significant and potentially adverse impact on our operations and financial condition. Our non-bank financial subsidiaries are also subject to various federal and state laws and regulations.

Holding Company Status and Acquisitions. The Company is a savings and loan holding company, as defined by federal banking law. We may not acquire control of another savings association unless the OTS approves such transaction and we may not be acquired by a company other than a bank holding company unless the OTS approves such transaction, or by an individual unless the OTS does not object after receiving notice. We may not be acquired by a bank holding company unless the Board of Governors of the Federal Reserve System (the "Federal Reserve") approves such transaction. In any case, the public must have an opportunity to comment on any such proposed acquisition and the OTS or Federal Reserve must complete an application review. Without prior approval from the OTS, we may not acquire more than 5% of the voting stock of any savings institution. In addition, the federal Gramm-Leach-Bliley Act generally restricts any non-financial entity from acquiring us unless such non-financial entity was, or had submitted an application to become, a savings and loan holding company on or before May 4, 1999. Also, because we were a savings and loan holding company prior to that date, we may engage in non-financial activities and acquire non-financial subsidiaries.

Capital Adequacy. The Bank must maintain a minimum amount of capital to satisfy various regulatory capital requirements under OTS regulations and federal law. There is no such requirement that applies to the Company. Federal law and regulations establish five levels of capital compliance: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. As of December 31, 2007, the Bank met all capital requirements to which it was subject and satisfied the requirements to be treated as "well-capitalized" under OTS regulations. An institution is treated as well-capitalized if its ratio of total risk-based capital to risk-weighted assets is 10.0% or more, its ratio of Tier 1 capital to risk-weighted assets is 6.0% or more, its leverage ratio (also referred to as its core capital ratio) is 5.0% or more, and it is not subject to any federal supervisory order or directive to meet a specific capital level. In contrast, an institution is only considered to be "adequately capitalized" if its capital structure satisfies lesser required levels, such as a total risk-based capital ratio of not less than 8.0%, a Tier 1 risk-based capital ratio of not less than 4.0%, and (unless it is in the most highly-rated category) a leverage ratio of not less than 4.0%. Any institution that is neither well capitalized nor adequately capitalized will be considered undercapitalized. Any institution with a tangible equity ratio of 2.0% or less will be considered critically undercapitalized.

On November 1, 2007, the OTS and the other U.S. banking agencies issued final regulations implementing the new risk-based regulatory capital framework developed by The Basel Committee on Banking Supervision, which is a working committee established by the central bank governors of certain industrialized nations, including the United States. The new risk-based regulatory capital framework, commonly referred to as Basel II, includes several methodologies for determining risk-based capital requirements, and the U.S. banking agencies have so far only adopted methodology known as the "advanced approach." The implementation of the advanced approach is mandatory for the largest U.S. banks and optional for other U.S. banks.

For those other U.S. banks, the U.S. banking agencies had issued advance rulemaking notices through December 2006 that contemplated possible modifications to the risk-based capital framework applicable to those domestic banking organizations that would not be affected by Basel II. These possible modifications, known colloquially as Basel 1A, were intended to avoid future competitive inequalities between Basel I and Basel II organizations. However, the U.S. banking agencies withdrew the proposed Basel 1A capital framework in late 2007. Instead, in 2008, the U.S. banking agencies announced that they would issue a proposed rule that would allow all U.S. banks not subject to the advanced approach under Basel II with the option of adopting a "standardized approach" under Basel II. Upon issuance of the proposed rule, we will assess the potential impact that it may have on our business practices as well as the broader competitive effects within the industry.

Qualified Thrift Lender. The Bank is required to meet a qualified thrift lender ("QTL") test to avoid certain restrictions on our operations, including the activities restrictions applicable to multiple savings and loan holding companies, restrictions on our ability to branch interstate and the Company's mandatory registration as a bank holding company under the Bank Holding Company Act of 1956. A savings association satisfies the QTL test if: (i) on a monthly average basis, for at least nine months out of each twelve month period, at least 65% of a specified asset base of the savings association consists of loans to small businesses, credit card loans, educational loans, or certain assets related to domestic residential real estate, including residential mortgage loans and mortgage securities; or (ii) at least 60% of the savings association's total assets consist of cash, U.S. government or government agency debt or equity securities, fixed assets, or loans secured by deposits, real property used for residential, educational, church, welfare, or health purposes, or real property in certain urban renewal areas. The Bank is currently, and expects to remain, in compliance with QTL standards.

Payment of Dividends. The Company is a legal entity separate and distinct from the Bank and our non-banking subsidiaries. The Company's principal sources of funds are cash dividends paid by the Bank and other subsidiaries, investment income and borrowings. Federal laws and regulations limit the amount of dividends or other capital distributions that the Bank may pay us. The Bank has an internal policy to remain "well-capitalized" under OTS capital adequacy regulations (discussed immediately above). Accordingly, the Bank does not currently expect to pay dividends to the Company if such payment would result in the Bank not being well capitalized. In addition, the Bank must seek prior approval from the OTS at least 30 days before it may make a capital distribution to the Company.

FDIC Assessment. The FDIC insures the deposits of the Bank and such insurance is backed by the full faith and credit of the United States government. Through March 31, 2006, the FDIC administered two separate deposit insurance funds, the Bank Insurance Fund (the "BIF") and the Savings Association Insurance Fund (the "SAIF"). The SAIF was the deposit insurance fund for most savings associations, including the Bank. In February 2006, President Bush signed into law the Federal Deposit Insurance Reform Conforming Amendments Act of 2005, which among other things allowed for the merger of the BIF and the SAIF to form the DIF. Under FDIC guidelines issued in November 2006, the Bank's premiums increased to increase the capitalization of the DIF. For 2007, the assessment was approximately $4.4 million, before any credits, as compared to $1.1 million in 2006.

If the Bank were to fail, claims for administrative expenses of the receiver and for deposits in all of our branches (including claims of the FDIC as subrogee) would have priority over the claims of general unsecured creditors and shareholders.

Affiliate Transaction Restrictions. The Bank is subject to the affiliate and insider transaction rules applicable to member banks of the Federal Reserve System as well as additional limitations imposed by the OTS. These provisions prohibit or limit a banking institution from extending credit to, or entering into certain transactions with, affiliates, principal stockholders, directors and executive officers of the banking institution and its affiliates.

Federal Reserve. Numerous regulations promulgated by the Federal Reserve affect the business operations of the Bank. These include regulations relating to equal credit opportunity, electronic fund transfers, collection of checks, truth in lending, truth in savings and availability of funds.

Under Federal Reserve Board regulations, the Bank is required to maintain a reserve against its transaction accounts (primarily interest-bearing and non-interest-bearing checking accounts). Because reserves must generally be maintained in cash or in non-interest-bearing accounts, the effect of the reserve requirement is to increase the Bank's cost of funds.

Patriot Act. The USA PATRIOT Act, which was enacted following the events of September 11, 2001, includes numerous provisions designed to detect and prevent international money laundering and to block terrorist access to the U.S. financial system. We have established policies and procedures intended to fully comply with the USA PATRIOT Act's provisions, as well as other aspects of anti-money laundering legislation and the Bank Secrecy Act.

Consumer Protection Laws and Regulations. Examination and enforcement by bank regulatory agencies for non-compliance with consumer protection laws and their implementing regulations have become more intense in nature. The Bank is subject to many federal consumer protection statutes and regulations, some of which are discussed below.

Federal regulations require extra disclosures and consumer protections to borrowers for certain lending practices. The term "predatory lending," much like the terms "safety and soundness" and "unfair and deceptive practices," is far-reaching and covers a potentially broad range of behavior. As such, it does not lend itself to a concise or a comprehensive definition. Predatory lending typically involves at least one, and perhaps all three, of the following elements:

- Making unaffordable loans based on the assets of the borrower rather than on the borrower's ability to repay an obligation ("asset-based lending");
- Inducing a borrower to refinance a loan repeatedly in order to charge high points and fees each time the loan is refinanced ("loan flipping"); and/or
- Engaging in fraud or deception to conceal the true nature of the loan obligation from an unsuspecting or unsophisticated borrower.

The federal Gramm-Leach-Bliley Act includes provisions that protect consumers from the unauthorized transfer and use of their non-public personal information by financial institutions. Privacy policies are required by federal banking regulations which limit the ability of banks and other financial institutions to disclose non-public personal information about consumers to nonaffiliated third parties. Pursuant to those rules, financial institutions must provide:

- Initial notices to customers about their privacy policies, describing the conditions under which they may disclose nonpublic personal information to nonaffiliated third parties and affiliates;
- Annual notices of their privacy policies to current customers; and
- A reasonable method for customers to "opt out" of disclosures to nonaffiliated third parties.

Many states also have predatory lending laws, and although the Bank is typically exempt from those laws due to federal preemption, they do apply to the brokers and correspondents from whom we purchase loans and, therefore have an effect on our business and our sales of certain loans into the secondary market.

These privacy protections affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. In addition, states are permitted under the Gramm-Leach-Bliley Act to have their own privacy laws, which may offer greater protection to consumers than the Gramm-Leach-Bliley Act. Numerous states in which we do business have enacted such laws.

The Fair Credit Reporting Act, as amended by the Fair and Accurate Credit Transactions Act, or FACT Act, requires financial firms to help deter identity theft, including developing appropriate fraud response programs, and gives consumers more control of their credit data. It also reauthorizes a federal ban on state laws that interfere with corporate credit granting and marketing practices. In connection with FACT Act, financial institution regulatory agencies proposed rules that would prohibit an institution from using certain information about a consumer it received from an affiliate to make a solicitation to the consumer, unless the consumer has been notified and given a chance to opt out of such solicitations. A consumer's election to opt out would be applicable for at least five years.

The Equal Credit Opportunity Act, or ECOA, generally prohibits discrimination in any credit transaction, whether for consumer or business purposes, on the basis of race, color, religion, national origin, sex, marital status, age (except in limited circumstances), receipt of income from public assistance programs, or good faith exercise of any rights under the Consumer Credit Protection Act.

The Truth in Lending Act, or TILA, is designed to ensure that credit terms are disclosed in a meaningful way so that consumers may compare credit terms more readily and knowledgeably. As a result of the TILA, all creditors must use the same credit terminology to express rates and payments, including the annual percentage rate, the finance charge, the amount financed, the total of payments and the payment schedule, among other things.

The Fair Housing Act, or FH Act, regulates many practices, including making it unlawful for any lender to discriminate in its housing-related lending activities against any person because of race, color, religion, national origin, sex, handicap or familial status. A number of lending practices have been found by the courts to be, or may be considered illegal under the FH Act, including some that are not specifically mentioned in the FH Act itself.

The Home Mortgage Disclosure Act, or HMDA, grew out of public concern over credit shortages in certain urban neighborhoods and provides public information that will help show whether financial institutions are serving the housing credit needs of the neighborhoods and communities in which they are located. The HMDA also includes a "fair lending" aspect that requires the collection and disclosure of data about applicant and borrower characteristics as a way of identifying possible discriminatory lending patterns and enforcing anti-discrimination statutes. In 2004, the Federal Reserve Board amended regulations issued under HMDA to require the reporting of certain pricing data with respect to higher-priced mortgage loans. This expanded reporting is being reviewed by federal banking agencies and others from a fair lending perspective.

The Real Estate Settlement Procedures Act, or RESPA, requires lenders to provide borrowers with disclosures regarding the nature and cost of real estate settlements. Also, RESPA prohibits certain abusive practices, such as kickbacks, and places limitations on the amount of escrow accounts.

Penalties under the above laws may include fines, reimbursements and other penalties. Due to heightened regulatory concern related to compliance with the FACT Act, ECOA, TILA, FH Act, HMDA and RESPA generally, the Bank may incur additional compliance costs or be required to expend additional funds for investments in its local community.

Community Reinvestment Act. The Community Reinvestment Act ("CRA") requires the Bank to ascertain and help meet the credit needs of the communities it serves, including low- to moderate-income neighborhoods, while maintaining safe and sound banking practices. The primary federal regulatory agency assigns one of four possible ratings to an institution's CRA performance and is required to make public an institution's rating and written evaluation. The four possible ratings of meeting community credit needs are outstanding, satisfactory, needs to improve and substantial noncompliance. In 2006, the Bank received an "outstanding" CRA rating from the OTS.

Regulatory Enforcement. Our primary federal banking regulator is the OTS. Both the OTS and the FDIC may take regulatory enforcement actions against any of their regulated institutions that do not operate in accordance with applicable regulations, policies and directives. Proceedings may be instituted against any banking institution, or any "institution-affiliated party," such as a director, officer, employee, agent or controlling person, who engages in unsafe and unsound practices, including violations of applicable laws and regulations. Both the OTS and the FDIC have authority under various circumstances to appoint a receiver or conservator for an insured institution that it regulates to issue cease and desist orders, to obtain injunctions restraining or prohibiting unsafe or unsound practices, to revalue assets and to require the establishment of reserves. The FDIC has additional authority to terminate insurance of accounts, after notice and hearing, upon a finding that the insured institution is or has engaged in any unsafe or unsound practice that has not been corrected, is operating in an unsafe or unsound condition or has violated any applicable law, regulation, rule, or order of, or condition imposed by, the FDIC.

Federal Home Loan Bank System. The primary purpose of the Federal Home Loan Banks (the "FHLBs") is to provide loans to their respective members in the form of collateralized advances for making housing loans as well as for affordable housing and community development lending. The FHLBs are generally able to make advances to their member institutions at interest rates that are lower than the members could otherwise obtain. The FHLB system consists of 12 regional FHLBs, each being federally chartered but privately owned by its respective member institutions. The Federal Housing Finance Board, a government agency, is generally responsible for regulating the FHLB system. The Bank is currently a member of the FHLB of Indianapolis.

Environmental Regulation

Our business and properties are subject to federal and state laws and regulations governing environmental matters, including the regulation of hazardous substances and wastes. For example, under the federal Comprehensive Environmental Response, Compensation, and Liability Act and similar state laws, owners and operators of contaminated properties may be liable for the costs of cleaning up hazardous substances without regard to whether such persons actually caused the contamination. Such laws may affect us both as an owner or former owner of properties used in or held for our business, and as a secured lender on property that is found to contain hazardous substances or wastes. Our general policy is to obtain an environmental assessment prior to foreclosing on commercial property. We may elect not to foreclose on properties that contain such hazardous substances or wastes, thereby limiting, and in some instances precluding, the liquidation of such properties.

Competition

We face substantial competition in attracting deposits and making loans. Our most direct competition for deposits has historically come from other savings institutions, commercial banks and credit unions in our local market areas. Money market funds and full-service securities brokerage firms also compete with us for deposits and, in recent years, many financial institutions have competed for deposits through the internet. We compete for deposits by offering high quality and convenient banking services at a large number of convenient locations, including longer banking hours and “sit-down” banking in which a customer is served at a desk rather than in a teller line. We may also compete by offering competitive interest rates on our deposit products.

From a lending perspective, there are a large number of institutions offering mortgage loans, consumer loans and commercial loans, including many mortgage lenders that operate on a national scale, as well as local savings institutions, commercial banks, and other lenders. We compete by offering competitive interest rates, fees and other loan terms and by offering efficient and rapid service.

Additional information

Our executive offices are located at 5151 Corporate Drive, Troy, Michigan 48098, and our telephone number is (248) 312-2000. Our stock is traded on the New York Stock Exchange under the symbol “FBC.”

We make our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act available free of charge on our website at www.flagstar.com as soon as reasonably practicable after we electronically file such material with the Securities and Exchange Commission. These reports are also available without charge on the SEC website at www.sec.gov.

ITEM 1A. RISK FACTORS

Our financial condition and results of operations may be adversely affected by various factors, many of which are beyond our control. These risk factors include the following:

General business, economic and political conditions may significantly affect our earnings.

Our business and earnings are sensitive to general business and economic conditions in the United States. These conditions include short-term and long-term interest rates, inflation, recession, unemployment, real estate values, fluctuations in both debt and equity capital markets, the value of the U.S. dollar as compared to foreign currencies, and the strength of the U.S. economy, as well as the local economies in which we conduct business. If any of these conditions worsen, our business and earnings could be adversely affected. For example, business and economic conditions that negatively impact household incomes could decrease the demand for our home loans and increase the number of customers who become delinquent or default on their loans; or, a rising interest rate environment could decrease the demand for loans.

In addition, our business and earnings are significantly affected by the fiscal and monetary policies of the federal government and its agencies. We are particularly affected by the policies of the Federal Reserve, which regulates the supply of money and credit in the United States, and the perception of those policies by the financial markets. The Federal Reserve's policies influence both the financial markets and the size and liquidity of the mortgage origination market, which significantly impacts the earnings of our mortgage lending operation and the value of our investment in MSRs and other retained interests. The Federal Reserve's policies and perceptions of those policies also influence the yield on our interest-earning assets and the cost of our interest-bearing liabilities. Changes in those policies or perceptions are beyond our control and difficult to predict and could have a material adverse effect on our business, results of operations and financial condition.

If we cannot effectively manage the impact of the volatility of interest rates, our earnings could be adversely affected.

Our main objective in managing interest rate risk is to maximize the benefit and minimize the adverse effect of changes in interest rates on our earnings over an extended period of time. In managing these risks, we look at, among other things, yield curves and hedging strategies. As such, our interest rate risk management strategies may result in significant earnings volatility in the short term because the market value of our assets and related hedges may be significantly impacted either positively or negatively by unanticipated variations in interest rates.

Our profitability depends in substantial part on our net interest margin, which is the difference between the rates we receive on loans made to others and investments and the rates we pay for deposits and other sources of funds. Our profitability also depends in substantial part on the volume of loan originations and the related fees received in our mortgage banking operations. Our net interest margin and our volume of mortgage originations will depend on many factors that are partly or entirely outside our control, including competition, federal economic, monetary and fiscal policies, and economic conditions generally. Historically, net interest margin and the mortgage origination volumes for the Bank and for other financial institutions have widened and narrowed in response to these and other factors. Our goal has been to structure our asset and liability management strategies to maximize the benefit of changes in market interest rates on our net interest margin and revenues related to mortgage origination volume. However, we can not give any assurance that a sudden or significant change in prevailing interest rates will not have a material adverse effect on our operating results.

We manage the strategic interest rate risk in our home lending operation primarily through the natural counterbalance of our loan production and servicing operations. Increasing long-term interest rates may decrease our mortgage loan originations and sales. Generally, the volume of mortgage loan originations is inversely related to the level of long-term interest rates. During periods of low long-term interest rates, a significant number of our customers may elect to refinance their mortgages (i.e., pay off their existing higher rate mortgage loans with new mortgage loans obtained at lower interest rates). Our profitability levels and those of others in the mortgage banking industry have generally been strongest during periods of low and/or declining interest rates, as we have historically been able to sell the resulting increased volume of loans into the secondary market at a gain. We have also benefited from periods of wide spreads between short and long term interest rates. If interest rates rise after we fix a price for a loan or commitment but before we close or sell such loan, the value of the loan will decrease and the amount we receive from selling the loan may be less than its cost to originate.

When interest rates fluctuate, repricing risks arise from the timing difference in the maturity and/or repricing of assets, liabilities and off-balance sheet positions. While such repricing mismatches are fundamental to our business, they can expose us to fluctuations in income and economic value as interest rates vary. Our interest rate risk management strategies do not completely eliminate repricing risk. A significant amount of our deposit liabilities are certificates of deposits, and these account holders may be more sensitive to the interest rate paid on their account than other depositors. There is no guarantee that in a changing rate environment we will be able to retain all of these depositors' accounts. We also call on local municipal agencies as another source for deposit funding. While a valuable source of liquidity, we believe that municipal deposits are usually extremely rate sensitive and, therefore, prone to withdrawal if higher interest rates are offered elsewhere. Because of the interest rate sensitivity of these depositors, there is no guarantee that in a changing rate environment we will be able to retain all funds in these accounts.

Changes in interest rates may cause a mismatch in our mortgage origination flow of loans, or “pipeline” and adversely affect our profitability. In our mortgage banking operation, we are exposed to interest rate risk from the time we commit to an interest rate on a mortgage loan application through the time we sell or commit to sell the mortgage loan. On a daily basis, we analyze various economic and market factors to estimate the percentage of mortgage loans we expect to sell for delivery at a future date. The amount of loans that we commit to sell is based in part on our expectation of the pull-through percentage, which is the ratio of mortgage loans closed divided by the number of mortgage loans on which we have issued binding commitments (and thereby locked in the interest rate) but have not yet closed (“pipeline loans”). If interest rates change in an unanticipated fashion, the actual percentage of pipeline loans that close may differ from the projected percentage. A mismatch of commitments to fund mortgage loans and commitments to sell mortgage loans may have an adverse effect on the results of operations in any such period. For instance, we may not have made commitments to sell these additional pipeline loans and therefore may incur significant losses upon their sale if the market rate of interest is higher than the mortgage interest rate to which we committed on such additional pipeline loans. Alternatively, we may have made commitments to sell more loans than actually closed or at prices that are no longer profitable to us. Our profitability may be adversely affected to the extent our economic hedging strategy for pipeline loans is not effective.

The value of our mortgage servicing rights could decline with reduction in interest rates.

The market value of, and earnings from, our mortgage loan servicing portfolio may be adversely affected by declines in interest rates. When mortgage rates rise we would generally expect payoffs in our servicing portfolio to decline, which generally should result in increases to the fair value of our MSRs. When mortgage interest rates decline, mortgage loan prepayments tend to increase as customers refinance their loans. When this happens, the income stream from our current mortgage loan servicing portfolio may decline. In that case, we may be required to amortize the portfolio over a shorter period of time or reduce the carrying value of our mortgage loan servicing portfolio.

Gains on Mortgage Servicing Rights May Be Difficult to Realize Due to Disruption in the Capital Markets.

Historically, we have sold mortgage servicing rights in secondary sales in order to realize profits, manage our capital levels and control interest rate risk. In the current environment, MSRs may be more difficult to sell, as many of the traditional buyers have exited the market due to a lack of capital availability, concern about housing prices or other reasons. If we do not sell MSRs, it could affect our profitability, result in increased capital requirements or require that we specifically hedge this asset.

We use estimates in determining the fair value of certain of our assets, which estimates may prove to be incorrect and result in significant declines in valuation.

A portion of our assets are carried on our statement of financial condition at fair value, including our initial capitalization of MSRs, trading assets and available for sale securities that represent certain retained interests from securitization activities, all other available-for-sale securities and derivatives. Generally, for assets that are reported at fair value, we use quoted market prices or internal valuation models that utilize observable market data inputs to estimate their fair value. In certain cases, observable market prices and data may not be readily available or their availability may be diminished due to market conditions. We use financial models to value certain of these assets. These models are complex and use asset specific collateral data and market inputs for interest rates. We cannot assure you that the models or the underlying assumptions will prove to be predictive and remain so over time, and therefore, actual results may differ from our models. Any assumptions we use are complex as we must make judgments about the effect of matters that are inherently uncertain and actual experience may differ from our assumptions. Different assumptions could result in significant declines in valuation, which in turn could result in significant declines in the dollar amount of assets we report on our statement of financial condition.

Current and further deterioration in the housing and commercial real estate markets may lead to increased loss severities and further worsening of delinquencies and non-performing assets in our loan portfolios. Consequently, our allowance for loan losses may not be adequate to cover actual losses, and we may be required to materially increase our reserves.

A significant source of risk arises from the possibility that we could sustain losses because borrowers, guarantors, and related parties may fail to perform in accordance with the terms of their loans. The underwriting and credit monitoring policies and procedures that we have adopted to address this risk may not prevent unexpected losses that could have an adverse effect on our business, financial condition, results of operations, cash flows and prospects. Unexpected losses may arise from a wide variety of specific or systemic factors, many of which are beyond our ability to predict, influence or control.

As with most lending institutions, we maintain an allowance for loan losses to provide for defaults and non-performance. Our allowance for loan losses may not be adequate to cover actual credit losses, and future provisions for credit losses could adversely affect our business, financial condition, results of operations, cash flows and prospects. The allowance for loan losses reflects our estimate of the probable losses in our portfolio of loans at the relevant statement of financial condition date. Our allowance for loan losses is based on prior experience as well as an evaluation of the risks in the current portfolio, composition and growth of the portfolio and economic factors. The determination of an appropriate level of loan loss allowance is an inherently difficult process and is based on numerous assumptions. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates, that may be beyond our control and these losses may exceed current estimates.

Recently, the housing and the residential mortgage markets have experienced a variety of difficulties and changed economic conditions. If market conditions continue to deteriorate, they may lead to additional valuation adjustments on our loan portfolios and real estate owned as we continue to reassess the market value of our loan portfolio, the loss severities of loans in default, and the net realizable value of real estate owned. Problems in the United States' residential real estate development industry could materially impact us. Poor economic conditions could result in decreased demand for residential housing, which, in turn, could adversely affect the development and construction efforts of residential real estate developers. Consequently, such economic downturns could adversely affect the ability of such residential real estate developer borrowers to repay these loans and the value of property used as collateral for such loans. Similar issues are arising in other markets, including commercial real estate. These problems faced by residential real estate developers and other commercial borrowers could have a material adverse impact on our financial results.

Our secondary market reserve for losses could be insufficient.

We currently maintain a secondary market reserve, which is a liability on our statement of financial condition, to reflect our best estimate of expected losses that we have incurred on loans that we have sold or securitized into the secondary market and must subsequently repurchase or with respect to which we must indemnify the purchasers because of violations of customary representations and warranties. Increases to this reserve for current loan sales reduce our net gain on loan sales, with adjustments to our previous estimates recorded as an increase or decrease to our other fees and charges. The level of the reserve reflects management's continuing evaluation of loss experience on repurchased loans, indemnifications, recovery history, and present economic conditions, among other things. The determination of the appropriate level of the secondary market reserve inherently involves a high degree of subjectivity and requires us to make significant estimates of repurchase risks and expected losses. Both the assumptions and estimates used could change materially, resulting in a level of reserve that is less than actual losses. Further, our bank regulators periodically review our secondary market reserve and may, in their discretion and based on their own judgment, which may differ from that of management, require us to increase the amount of the reserve through additional provisions. Such increases will result in a reduction in net earnings and could have an adverse effect on our statement of financial condition and results of operations.

Our home lending profitability could be significantly reduced if we are not able to resell mortgages.

Currently, we sell a substantial portion of the mortgage loans we originate. The profitability of our mortgage banking operations depends in large part upon our ability to aggregate a high volume of loans and to sell them in the secondary market at a gain. Thus, we are dependent upon (1) the existence of an active secondary market and (2) our ability to profitably sell loans or securities into that market.

Our ability to sell mortgage loans readily is dependent upon the availability of an active secondary market for single-family mortgage loans, which in turn depends in part upon the continuation of programs currently offered by Fannie Mae, Freddie Mac, Ginnie Mae and other institutional and non-institutional investors. These entities account for a substantial portion of the secondary market in residential mortgage loans. Some of the largest participants in the secondary market, including Fannie Mae, Freddie Mac and Ginnie Mae, are government-sponsored enterprises whose activities are governed by federal law. Any future changes in laws that significantly affect the activity of such government-sponsored enterprises could, in turn, adversely affect our operations.

In addition, our ability to sell mortgage loans readily is dependent upon our ability to remain eligible for the programs offered by Fannie Mae, Freddie Mac, Ginnie Mae and other institutional and non-institutional investors. We expect to remain eligible to participate in such programs, but any significant impairment of our eligibility could materially and adversely affect our operations. Further, the criteria for loans to be accepted under such programs may be changed from time-to-time by the sponsoring entity. The profitability of participating in specific programs may vary depending on a number of factors, including our administrative costs of originating and purchasing qualifying loans.

Our commercial real estate and commercial business loan portfolios carry heightened credit risk.

In recent years, we have emphasized the origination of commercial real estate and commercial business loans. At December 31, 2007, our balance of commercial loans was $1.6 billion, which was 19.8% of loans held for investment and 10.1% of total assets. Loans collateralized by commercial real estate are generally thought to have a greater degree of credit risk than single-family residential mortgage loans and carry larger loan balances. This increased credit risk is a result of several factors, including the concentration of principal in a limited number of loans and borrowers, the effects of general economic conditions on income-producing properties, and the greater difficulty of evaluating and monitoring these types of loans.

Furthermore, the repayment of loans collateralized by commercial real estate is typically dependent upon the successful operation of the related real estate property. If the cash flow from the project is reduced, the borrower’s ability to repay the loan may be impaired. Other commercial business loans generally have a greater credit risk than residential mortgage loans as well. Conversely, residential mortgage loans are generally made on the basis of the borrower’s ability to make repayment from his or her employment or other income, and are secured by real property whose value tends to be more easily ascertainable. As a result, the availability of funds for the repayment of commercial business loans may depend substantially on the success of the business itself. Further, any collateral securing the loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

We have substantial risks in connection with securitizations and loan sales.

Securitization and loan sale transactions comprise a significant source of our overall funding. Our sales channels include whole loan sales, sales to government-sponsored enterprises and sales through private-label securitizations. Private-label securitizations, sponsored by us, involve transfers of loans to off-balance sheet qualifying special purpose entities, which in turn issue securities to third parties.

In a securitization transaction, we may recognize a gain or loss on sale resulting from related residuals and/or servicing rights in the securitized pool of loans when we sell or securitize the assets. The values assigned to the residuals and/or servicing assets depends upon certain assumptions that we make about the future performance of the securitized loan portfolio, including the level of credit losses and the rate of prepayments. Residuals, which are retained interests created in a mortgage loan securitization, typically represent the first loss position and are not typically rated by a nationally recognized rating agency. If we hold the residuals, we are at risk for the initial losses that occur with these securitizations. Decreases in the value of the residuals and/or servicing assets in securitizations that we have completed due to market interest rate fluctuations, higher than expected credit losses on prepayments, or changes in the volume of assets securitized or sold due to our inability to access the asset-backed securitization markets or other funding sources could have a material adverse effect on our business, financial condition and results of operations.

Our ability to borrow funds and raise capital could be limited, which could adversely affect our earnings.

Our access to external sources of financing, as well as the cost of that financing, is dependent on various factors and could be adversely affected by a deterioration of our credit ratings including our servicer rating, which are influenced by a number of factors. These include, but are not limited to: material changes in operating margins; earnings trends and volatility; the prudence of funding and liquidity management practices; financial leverage on an absolute basis or relative to peers; the composition of the statement of financial condition and/or capital structure; geographic and business diversification; and our market share and competitive position in the business segments in which we operate. Material deterioration in any one or a combination of these factors could result in a downgrade of our credit or servicer ratings, thus increasing the cost of and/or limiting the availability of unsecured financing. A reduction in our credit rating or servicing rating could cause the loss of custodial deposits for our agency servicing portfolio.

Our ability to make mortgage loans depends largely on our ability to secure funds on terms acceptable to us. Our primary sources of funds to meet our financing needs include loan sales and securitizations, deposits, which include custodial amounts from our agency servicing portfolio, borrowings from the FHLB, borrowings from investment and commercial banks through repurchase agreements, and capital-raising activities. Our ability to maintain borrowing facilities is subject to renewal of these facilities. If we are unable to renew any of these financing arrangements or arrange for new financing on terms acceptable to us, or if we default on any of the restrictions imposed upon us by our borrowing facilities, then we may have to reduce the number of loans we are able to originate for sale in the secondary market or for our own investment. A sudden and significant reduction in loan originations that occurs as a result could adversely impact our earnings. There is no guarantee that we will be able to adequately access capital markets when or if a need for additional capital arises.

We may be required to raise capital at terms that are materially adverse to our shareholders.

We suffered a loss in excess of $39 million during 2007 and as a result, saw our shareholders' equity and regulatory capital decline in the second half of the year. While we currently have regulatory capital ratios in excess of the "well capitalized" requirement, there can be no assurance that we will not suffer additional losses or that additional capital will not otherwise be required for regulatory or other reasons. In those circumstances, we may be required to obtain additional capital to maintain our regulatory capital ratios at the "well capitalized" level. Such capital raising could be at terms that are dilutive to existing shareholders and there can be no assurance that any capital raising we undertake would be successful given the current level of disruption in financial markets.

Our holding company is dependent on the Bank for funding of obligations and dividends.

As a holding company without significant assets other than the capital stock of the Bank, the Company's ability to service its debt, including payment of interest on debentures issued as part of capital raising activities using trust preferred securities or pay dividends to stockholders, is dependent upon the receipt of dividends from the Bank on such capital stock. The declaration of dividends by the Bank on all classes of its capital stock is subject to the discretion of the Board of Directors of the Bank and to applicable regulatory limitations. If the earnings of the Company's subsidiaries are not sufficient to make dividend payments to the Company while maintaining adequate capital levels, the Company may not be able to make dividend payments to its common shareholders or service its debt. See "Item 1. Business — Regulation and Supervision — Payment of Dividends."

We may not be able to replace key members of senior management or attract and retain qualified relationship managers in the future.

We depend on the services of existing senior management to carry out our business and investment strategies. As we expand and as we continue to refine our business model, we will need to continue to attract and retain additional senior management and to recruit qualified individuals to succeed existing key personnel that leave our employ. In addition, as we continue to grow our business and plan to continue to expand our locations, products and services, we will need to continue to attract and retain qualified banking personnel. Competition for such personnel is especially keen in our geographic market areas and competition for the best people in most businesses in which we engage can be intense. If we are unable to attract and retain talented people, our business could suffer. The loss of the services of any senior management personnel, or the inability to recruit and retain qualified personnel in the future, could have an adverse effect on our results of operations, financial conditions and prospects.

The network and computer systems on which we depend could fail or experience a security breach.

Our computer systems could be vulnerable to unforeseen problems. Because we conduct part of our business over the Internet and outsource several critical functions to third parties, operations will depend on the ability, as well as that of third-party service providers, to protect computer systems and network infrastructure against damage from fire, power loss, telecommunications failure, physical break-ins or similar catastrophic events. Any damage or failure that causes interruptions in operations could have a material adverse effect on our business, financial condition and results of operations.

In addition, a significant barrier to online financial transactions is the secure transmission of confidential information over public networks. Our Internet banking system relies on encryption and authentication technology to provide the security and authentication necessary to effect secure transmission of confidential information. Advances in computer capabilities, new discoveries in the field of cryptography or other developments could result in a compromise or breach of the algorithms our third-party service providers use to protect customer transaction data. If any such compromise of security were to occur, it could have a material adverse effect on our business, financial condition and results of operations.

Market acceptance of Internet banking depends substantially on widespread adoption of the Internet for general commercial and financial services transactions. If another provider of commercial services through the Internet were to suffer damage from physical break-in, security breach or other disruptive problems caused by the Internet or other users, the growth and public acceptance of the Internet for commercial transactions could suffer. This type of event could deter our potential customers or cause customers to leave us and thereby materially and adversely affect our business, financial condition and results of operations.

Our business is highly regulated.

The banking industry is extensively regulated at the federal and state levels. Insured depository institutions and their holding companies are subject to comprehensive regulation and supervision by financial regulatory authorities covering all aspects of their organization, management and operations. The OTS is the primary regulator of the Bank and its affiliated entities. In addition to its regulatory powers, the OTS also has significant enforcement authority that it can use to address unsafe and unsound banking practices, violations of laws, and capital and operational deficiencies. Such regulation and supervision are intended primarily for the protection of the insurance fund and for our depositors and borrowers, and are not intended to protect the interests of investors in our common stock. Further, the Bank's business is affected by consumer protection laws and regulation at the state and federal level, including a variety of consumer protection provisions, many of which provide for a private right of action and pose a risk of class action lawsuits. Accordingly, the actions of governmental authorities responsible for regulatory, fiscal and monetary affairs can have a significant and immediate impact on the activities of financial services firms such as ours. See further information in "Item 1. Business — Regulation and Supervision."

Our business has volatile earnings because it operates based on a multi-year cycle.

The home lending segment of our business is a cyclical business that generally performs better in a low interest rate environment with a yield curve that is lower at the shorter time frames and higher at the longer time frames. In addition, other external factors, including tax laws, the strength of various segments of the economy and demographics of our lending markets, could influence the level of demand for mortgage loans. Gain on sale of loans is a large component of our revenue and could be adversely impacted by a significant decrease in the volume of our mortgage loan originations to the extent the effect of the volume decline is not offset by an increase in the profit margins on such loans sales.

Our loans are geographically concentrated in only a few states.

A significant portion of our mortgage loan portfolio is geographically concentrated in certain states, including California, Michigan, Florida, Washington, Colorado, Texas and Arizona, which collectively represent approximately 67.3% of our mortgage loans held for investment balance at December 31, 2007. In addition, 63.1% of our commercial real estate loans are in Michigan. Continued adverse economic conditions in these few markets could cause delinquencies and charge-offs of these loans to increase, likely resulting in a corresponding and disproportionately large decline in revenues and an increase in credit risk. Also, we could be adversely affected by business disruptions triggered by natural disasters, or acts of war or terrorism.

A large percentage of our loans are collateralized by real estate, and an adverse change in the real estate market may result in losses and adversely affect our portfolio.

Approximately 96.3% of our investment loan portfolio as of December 31, 2007, was comprised of loans collateralized by real estate. The collateral in each case provides an alternate source of repayment if the borrower defaults and may deteriorate in value during the time the credit is extended. Adverse changes in the economy affecting real estate values may have significantly impaired the value of our collateral as well as our ability to even sell the collateral upon foreclosure, particularly with respect to our loans with second liens. If the collateral is sold in the event of a default with respect to any of these loans, amounts received may be insufficient to recover all of the outstanding principal and uncollected interest on the loan. As a result, our profitability could continue to be negatively impacted by adverse changes in the real estate market.

A significant part of our business strategy involves adding new branch locations, and our failure to grow may adversely affect our business, prospects, results of operations and financial condition.

Our expansion strategy consists principally of adding new branch locations in Michigan and Georgia growth areas that complement our existing branch network. While we anticipate that this expansion strategy will enhance long-term shareholder value, it is possible that our branch expansion strategy may not become accretive to our earnings over the short term. New branches generally require a significant initial capital investment for land and building expenses and take several years to become profitable. Accordingly, we anticipate that, in the short term, net operations will be negatively affected as we incur significant capital expenditures and noninterest expense in opening and operating new branches before the new branches can produce sufficient net interest income to offset the increased expense. In addition, the need to use capital to fund de novo branching may limit our ability to increase our interest-earning assets, generate MSRs or to pay or increase dividends on our common stock. There also is implementation risk associated with new branches. Numerous factors will determine whether our branch expansion strategy will be successful, such as our ability to select suitable branch locations, real estate acquisition costs, competition, interest rates, managerial resources, our ability to hire and retain qualified personnel, the effectiveness of our marketing strategy and our ability to attract deposits.

We are subject to heightened regulatory scrutiny with respect to bank secrecy and anti-money laundering statutes and regulations.

In recent years, regulators have intensified their focus on the USA PATRIOT Act's anti-money laundering and Bank Secrecy Act compliance requirements. There is also increased scrutiny of our compliance with the rules enforced by the Office of Foreign Assets Control. In order to comply with regulations, guidelines and examination procedures in this area, we have been required to adopt new policies and procedures and to install new systems. We can not be certain that the policies, procedures and systems we have in place are flawless. Therefore, there is no assurance that in every instance we are in full compliance with these requirements.

Other Risk Factors.

The above description of risk factors is not exhaustive. Other risk factors are described elsewhere herein as well as in other reports and documents that we file with or furnish to the SEC. Other factors that could also cause results to differ from our expectations may not be described in any such report or document. Each of these factors could by itself, or together with one or more other factors, adversely affect our business, results of operations and/or financial condition.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

At December 31, 2007, we operated from the headquarters in Troy, Michigan, a regional office in Jackson, Michigan, and a regional office in Atlanta, Georgia, 164 banking centers in Michigan, Indiana and Georgia and 143 home lending centers in 27 states. We also maintain 13 wholesale lending offices. Our banking centers consist of 97 free-standing office buildings, 41 in-store banking centers and 26 centers in buildings in which there are other tenants, typically strip malls and similar retail centers.

We own the buildings and land for 87 of our offices, own the building but lease the land for one of our offices, and lease the remaining 232 offices. The offices that we lease have lease expiration dates ranging from 2008 to 2017.

ITEM 3. LEGAL PROCEEDINGS

From time to time, we are party to legal proceedings incident to our business. However, at December 31, 2007, there were no legal proceedings that we anticipate will have a material adverse effect on us. See Note 19 of the Notes to Consolidated Financial Statements in Item 8. Financial Statements and Supplementary Data.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No items were submitted during the fourth quarter of the year covered by this annual report of Form 10-K to be voted on by security holders through a solicitation of proxies or otherwise.

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our common stock trades on the New York Stock Exchange under the trading symbol FBC. At December 31, 2007, there were 60,270,624 shares of our common stock outstanding held by approximately 14,400 shareholders of record.

Dividends

The following table shows the high and low closing prices for the Company's common stock during each calendar quarter during 2007 and 2006, and the cash dividends per common share declared during each such calendar quarter. We have declared dividends on our common stock on a quarterly basis in the past. However, the amount of and nature of any dividends declared on our common stock in the future will be determined by our Board of Directors in their sole discretion. In their meeting on February 19, 2008, our Board of Directors suspended any future dividend on our common stock until the capital markets normalize and residential real estate shows signs of improvement.

Quarter Ending	Highest Closing Price	Closing Lowest Price	Dividends Declared in the Period
December 31, 2007	$10.23	$ 5.90	$0.05
September 30, 2007	$13.08	$ 9.73	$0.10
June 30, 2007	$13.43	$11.30	$0.10
March 31, 2007	$14.96	$11.95	$0.10
December 31, 2006	$15.46	$14.31	$0.15
September 30, 2006	$16.29	$14.01	$0.15
June 30, 2006	$16.96	$14.67	$0.15
March 31, 2006	$15.60	$14.08	$0.15

Equity Compensation Plan Information

The following table sets forth certain information with respect to securities to be issued under the Company's equity compensation plans as of December 31, 2007.

Plan Category	Number of Securities to Be Issued Upon Exercise of Outstanding Options	Weighted-Average Exercise Price of Outstanding Options	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans
Equity Compensation Plans approved by security holders (1)	2,697,997	$14.04	5,236,705
Total	2,697,997	$14.04	5,236,705

(1) Consists of our 2006 Equity Incentive Plan, which provides for the granting of stock options, incentive stock options, cash-settled stock appreciation rights, restricted stock units, performance shares and performance units and other awards. The 2006 Equity Incentive Plan consolidated, merged, amended and restated our 1997 Employees and Directors Stock Option Plan, 2000 Stock Incentive Plan, and 1997 Incentive Compensation Plan. Awards still outstanding under any of the prior plans will continue to be governed by their respective terms. Under the 2006 Equity Incentive Plan, the exercise price of any option granted must be at least equal to the fair value of our common stock on the date of grant. Non-qualified stock options granted to directors expire five years from the date of grant. Grants other than non-qualified stock options have term limits set by the Board of Directors in the applicable agreement. All securities remaining for future issuance represent option and stock awards available for award under the 2006 Equity Incentive Plan.

Sale of Unregistered Securities

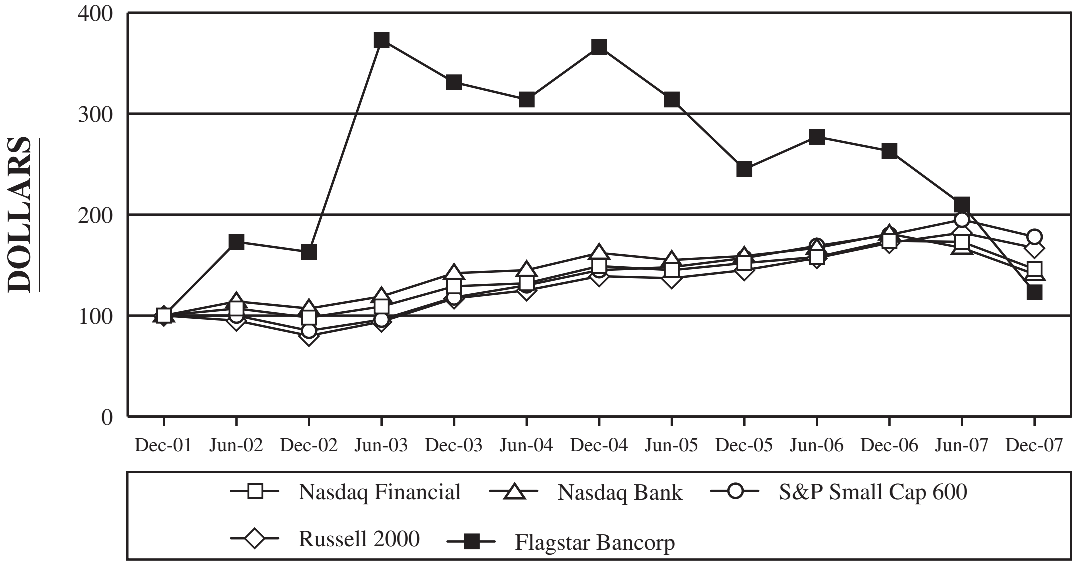
The Company made no unregistered sales of its common stock during the quarter ended December 31, 2007.

Issuer Purchases of Equity Securities

There were no shares of our common stock that we purchased in the fourth quarter of 2007.

On January 31, 2007, the Company announced that the Board of Directors had adopted a Stock Repurchase Program under which the Company was authorized to repurchase up to $40.0 million worth of outstanding common stock. On February 27, 2007, the Company announced that the Board of Directors had increased the authorized repurchase amount to $50.0 million. On April 26, 2007, the Board increased the authorized repurchase amount to $75.0 million. This program expired on January 31, 2008. For the year ended December 31, 2007, $41.7 million was used to repurchase 3.4 million shares under the program.

CUMULATIVE TOTAL STOCKHOLDER RETURN
COMPARED WITH PERFORMANCE OF SELECTED INDICES
DECEMBER 31, 2001 THROUGH DECEMBER 31, 2007



	Dec-01	Jun-02	Dec-02	Jun-03	Dec-03	Jun-04	Dec-04	Jun-05	Dec-05	Jun-06	Dec-06	Jun-07	Dec-07
Nasdaq Financial	100	107	98	109	129	132	149	145	152	158	174	173	146
Nasdaq Bank	100	114	107	119	142	145	162	155	159	167	181	167	141
S&P Small Cap 600	100	100	85	96	118	130	145	148	157	169	180	195	178
Russell 2000	100	95	80	94	117	125	139	137	145	157	172	182	167
Flagstar Bancorp	100	173	163	373	331	314	366	314	245	277	263	210	123

ITEM 6. SELECTED FINANCIAL DATA

	For the Years Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands, except per share data and percentages)				
Summary of Consolidated Statements of Operations:					
Interest income	$905,509	$800,866	$708,663	$563,437	$503,068
Interest expense	695,631	585,919	462,393	340,146	308,482
Net interest income	209,878	214,947	246,270	223,291	194,586
Provision for loan losses	88,297	25,450	18,876	16,077	20,081
Net interest income after provision for loan losses	121,581	189,497	227,394	207,214	174,505
Other income	117,115	202,161	159,448	256,121	465,877
Operating and administrative expenses	297,510	275,637	262,887	243,005	252,915
(Loss) earnings before federal income tax provision	(58,814)	116,021	123,955	220,330	387,467
(Benefit) provision for federal income taxes	(19,589)	40,819	44,090	77,592	135,481
Net (loss) earnings	$ (39,225)	$ 75,202	$ 79,865	$142,738	$251,986
(Loss) earnings per share					
Basic	$ (0.64)	$ 1.18	$ 1.29	$ 2.34	$ 4.21
Diluted	$ (0.64)	$ 1.17	$ 1.25	$ 2.22	$ 3.95
Dividends per common share	$ 0.35	$ 0.60	$ 0.90	$ 1.00	$ 0.50
Dividend payout ratio	N/M	51%	70%	43%	11%

Note: N/M — not meaningful.

	At or for the Years Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands, except per share data and percentages)				
Summary of Consolidated Statements of Financial Condition:					
Total assets	$15,792,736	$15,497,205	$15,075,430	$13,143,014	$10,553,246
Mortgage-backed securities held to maturity	1,255,431	1,565,420	1,414,986	20,710	30,678
Loans receivable	11,645,707	12,128,480	12,349,865	12,065,465	9,599,803
Mortgage servicing rights	413,986	173,288	315,678	187,975	260,128
Total deposits	8,236,744	7,623,488	8,521,756	7,433,776	5,729,650
FHLB advances	6,301,000	5,407,000	4,225,000	4,090,000	3,246,000
Security repurchase agreements	108,000	990,806	1,060,097	—	—
Stockholders' equity	692,978	812,234	771,883	728,954	638,801
Other Financial and Statistical Data					
Tangible capital ratio	5.78%	6.37%	6.26%	6.19%	7.34%
Core capital ratio	5.78%	6.37%	6.26%	6.19%	7.34%
Total risk-based capital ratio	10.66%	11.55%	11.09%	10.97%	13.30%
Equity-to-assets ratio (at the end of the period)	4.39%	5.24%	5.12%	5.54%	6.05%
Equity-to-assets ratio (average for the period)	4.48%	5.29%	5.07%	5.68%	5.17%
Book value per share	$ 11.50	$ 12.77	$ 12.21	$ 11.88	$ 10.53
Shares outstanding	60,271	63,605	63,208	61,358	60,675
Average shares outstanding	61,152	63,504	62,128	61,057	59,811
Mortgage loans originated or purchased	$25,711,438	$18,966,354	$28,244,561	$34,248,988	$56,550,735
Other loans originated or purchased	981,762	1,241,588	1,706,246	995,429	609,092
Loans sold	24,255,114	16,370,925	23,451,430	28,937,576	51,922,757
Mortgage loans serviced for others	32,487,337	15,032,504	29,648,088	21,354,724	30,395,079
Capitalized value of mortgage servicing rights	1.27%	1.15%	1.06%	0.88%	0.86%
Interest rate spread — consolidated	1.33%	1.42%	1.74%	1.87%	2.01%
Net interest margin — consolidated	1.40%	1.54%	1.82%	1.99%	2.16%
Interest rate spread — bank only	1.39%	1.41%	1.68%	1.85%	1.91%
Net interest margin — bank only	1.50%	1.63%	1.88%	2.08%	2.40%
Return on average assets	(0.24)%	0.49%	0.54%	1.17%	2.50%
Return on average equity	(5.14)%	9.42%	10.66%	20.60%	48.35%
Efficiency ratio	91.0%	66.1%	64.8%	50.7%	38.3%
Net charge off ratio	0.35%	0.20%	0.16%	0.16%	0.35%
Ratio of allowance to investment loans	1.28%	0.51%	0.37%	0.36%	0.55%
Ratio of non-performing assets to total assets	2.00%	1.03%	0.98%	0.99%	1.01%
Ratio of allowance to non-performing loans	52.8%	80.2%	60.7%	67.2%	64.9%
Number of banking centers	164	151	137	120	98
Number of home loan centers	143	76	101	112	128

Note: All per share data has been restated for the 2 for 1 stock split on May 15, 2003.

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

Overview

Operations of the Bank are categorized into two business segments: banking and home lending. Each segment operates under the same banking charter, but is reported on a segmented basis for financial reporting purposes. For certain financial information concerning the results of operations of our banking and home lending operations, see Note 26 of the Notes to Consolidated Financial Statements, in Item 8, Financial Statements, herein.

Banking Operation. We provide a full range of banking services to consumers and small businesses in Michigan, Indiana and Georgia. Our banking operation involves the gathering of deposits and investing those deposits in duration-matched assets consisting primarily of mortgage loans originated by our home lending operation. The banking operation holds these loans in its loans held for investment portfolio in order to earn income based on the difference, or "spread," between the interest earned on loans and investments and the interest paid for deposits and other borrowed funds. At December 31, 2007, we operated a network of 164 banking centers and provided banking services to approximately 122,704 customers. We continue to focus on expanding our branch network in order to increase our access to retail deposit funding sources. As we open new branches, we believe that the growth in deposits will continue over time. During 2007, we opened 13 banking centers, including six banking centers in Georgia. During 2007, we expect to open seven additional branches in the Atlanta, Georgia area and five branches in Michigan.

Home Lending Operation. Our home lending operation originates, securitizes and sells residential mortgage loans in order to generate transactional income. The home lending operation also services mortgage loans on a fee basis for others and sells mortgage servicing rights into the secondary market. Funding for our home lending operation is provided primarily by deposits and borrowings obtained by our banking operation.

The following tables present certain financial information concerning the results of operations of our banking operation and home lending operation during the past three years.

BANKING OPERATION

	At or for the Years Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net interest income	$ 99,984	$ 159,255	$ 185,276
Net gain on sale revenue	—	—	—
Other income	27,868	31,353	55,813
(Loss) earnings before federal taxes	(74,247)	59,728	123,726
Identifiable assets	$15,014,734	$14,939,341	$14,176,340

HOME LENDING OPERATION

	At or for the Years Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Net interest income	$ 109,894	$ 55,692	$ 60,994
Net gain on sale revenue	64,928	135,002	81,737
Other income	24,319	35,806	21,898
Earnings before federal taxes	15,433	56,293	229
Identifiable assets	$4,188,002	$3,597,864	$2,379,090

Summary of Operations

Our net loss for 2007 of ($39.2) million (loss of $0.64 per diluted share) represents a 152.1% decrease from the earnings of $75.2 million ($1.17 per diluted share) we achieved in 2006 and a decrease of 149.1% from the $79.9 million ($1.25 per diluted share) earned in 2005. The net loss during 2007 was affected by the following factors:

- Higher provision for loan losses due to an increase in delinquency rates and non-performing loans;
- Lower gain on sales of MSRs due to substantially lower volume of MSR sales;
- Higher gain on loan sales due to increased volume and a slight decrease in overall gain on sale spread;
- Impairment losses in residual interests and securities;
- Lower net interest income due to the increase in the average interest rate that we paid on our deposits and interest-bearing liabilities offset by a lower average interest rate that we earned on our interest-earning assets;
- Higher overhead costs in our banking group attributable in part to the 13 additional banking centers that were opened during the year as well as 14 banking centers opened in 2006 as part of our overall de novo branch bank strategy; and
- Higher overhead costs in our home lending operation due to an increase in the number of salaried and commissioned personnel attributable to an increase of 67 home loan centers opened during the year as we focused on increasing our retail lending capability.

See "Results of Operations" below.

Critical Accounting Policies

Our consolidated financial statements are prepared in accordance with U.S. GAAP and reflect general practices within our industry. Application of these principles requires management to make estimates or judgments that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates are based on information available to management as of the date of the consolidated financial statements. Accordingly, as this information changes, future financial statements could reflect different estimates or judgments. Certain policies inherently have a greater reliance on the use of estimates, and as such have a greater possibility of producing results that could be materially different than originally reported. The most significant accounting policies followed by us are presented in Note 2 to the consolidated financial statements included in Item 8 herein. These policies, along with the disclosures presented in the other financial statement notes and other information presented herein, provide information on how significant assets and liabilities are valued in the consolidated financial statements and how these values are determined. Management views critical accounting policies to be those that are highly dependent on subjective or complex judgments, estimates or assumptions, and where changes in those estimates and assumptions could have a significant impact on our consolidated financial statements. Management currently views the determination of the allowance for loan losses, the valuation of MSRs, the valuation of residuals, the valuation of derivative instruments, and the determination of the secondary market reserve to be our critical accounting policies.

Allowance for Loan Losses. The allowance for loan losses represents management's estimate of probable losses that are inherent in our loans held for investment portfolio, but which have not yet been realized as of the date of our consolidated statement of financial condition. We recognize these losses when (a) available information indicates that it is probable that a loss has occurred and (b) the amount of the loss can be reasonably estimated. We believe that the accounting estimates related to the allowance for loan losses are critical because they require us to make subjective and complex judgments about the effect of matters that are inherently uncertain. As a result, subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for loan losses. Our methodology for assessing the adequacy of the allowance involves a significant amount of judgment based on various factors such as general economic and business conditions, credit quality and collateral value trends, loan concentrations, recent trends in our loss experience, new product initiatives and other variables. Although management believes its process for determining the allowance for loan losses adequately considers all of the factors that could potentially result in loan losses, the process includes subjective elements and may be susceptible to significant change. To the extent actual outcomes differ from management estimates, additional provision for loan losses could be required that could adversely affect operations or financial position in future periods.

Valuation of Mortgage Servicing Rights. When our home lending operation sells mortgage loans in the secondary market it usually retains the right to continue to service these loans and earn a servicing fee. At the time the loan is sold on a servicing retained basis, we record the mortgage servicing right as an asset at its fair value. Determining the fair value of MSRs involves a calculation of the present value of a set of market driven and MSR specific cash flows. MSRs do not trade in an active market with readily observable market prices. However, the market price of MSRs is generally a function of demand and interest rates. When mortgage interest rates decline, mortgage loan prepayments usually increase as customers refinance their loans. When this happens, the income stream from a MSR portfolio will decline. In that case, we may be required to amortize the portfolio over a shorter period of time or reduce the carrying value of our MSR portfolio. Accordingly, we must make assumptions about future interest rates and other market conditions in order to estimate the current fair value of our MSR portfolio. On an ongoing basis, we compare our fair value estimates to observable market data where available. On an annual basis, the value of our MSR portfolio is reviewed by an outside valuation expert. MSRs are recorded at the lower of carrying cost or fair market value.

From time to time, we sell some of these MSRs to unaffiliated purchasers in transactions that are separate from the sale of the underlying loans. At the time of the sale, we record a gain or loss based on the selling price of the MSRs less our carrying value and associated transaction costs.

Valuation of Residuals. Residuals are created upon the issuance of private-label securitizations. Residuals represent the first loss position and are not typically rated by the nationally recognized agencies. The value of residuals represents the present value of the future cash flows expected to be received by us from the excess cash flows created in the securitization transaction. In general, future cash flows are estimated by taking the coupon rate of the loans underlying the transaction less the interest rate paid to the investors, less contractually specified servicing and trustee fees adjusting for the effect of estimated prepayments and credit losses.

Cash flows are also dependent upon various restrictions and conditions specified in each transaction. For example, residual securities are not typically entitled to any cash flows unless over-collateralization has reached a certain level. The over-collateralization represents the difference between the bond balance and the collateral underlying the security. A sample of an over-collateralization structure may require 2% of the original collateral balance for 36 months. At month 37, it may require 4%, but on a declining balance basis. Due to prepayments, that 4% requirement is generally less than the 2% required on the original balance. In addition, the transaction may include an over-collateralization "trigger event," the occurrence of which may require the over-collateralization to be increased. An example of such trigger event is delinquency rates or cumulative losses on the underlying collateral that exceed stated levels. If over-collateralization targets were not met, the trustee would apply cash flows that would otherwise flow to the residual security until such targets are met. A delay or reduction in the cash flows received will result in a lower valuation of the residual.

Residuals are designated as either available-for-sale or trading securities at the time of securitization and are periodically evaluated for impairment. These residuals are marked to market with changes in the value either recognized in other comprehensive income net of tax for available-for-sale securities or earnings for trading securities. If the available-for-sale security is deemed to be impaired and the impairment is other-than-temporary, the impairment is recognized in the current period earnings. We use an internally developed model to value the residuals. The model takes into consideration the cash flow structure specific to each transaction (such as over-collateralization requirements and trigger events). The key valuation assumptions include credit losses, prepayment rates and, to a lesser degree, discount rates.

Valuation of Derivative Instruments. We utilize certain derivative instruments in the ordinary course of our business to manage our exposure to changes in interest rates. These derivative instruments include forward sale commitments and interest rate swaps. We also issue interest rate lock commitments to borrowers in connection with single family mortgage loan originations. We recognize all derivative instruments on our consolidated statement of financial position at fair value. The valuation of derivative instruments is considered critical because many are valued using discounted cash flow modeling techniques in the absence of market value quotes. Therefore, we must make estimates regarding the amount and timing of future cash flows, which are susceptible to significant change in future periods based on changes in interest rates. Our interest rate assumptions are based on current yield curves, forward yield curves and various other factors. Internally generated valuations are compared to third party data where available to validate the accuracy of our valuation models.

Derivative instruments may be designated as either fair value or cash flow hedges under hedge accounting principles or may be undesignated. A hedge of the exposure to changes in the fair value of a recognized asset, liability or unrecognized firm commitment is referred to as a fair value hedge. A hedge of the exposure to the variability of cash flows from a recognized asset, liability or forecasted transaction is referred to as a cash flow hedge. In the case of a qualifying fair value hedge, changes in the value of the derivative instruments that are highly effective are recognized in current earnings along with the changes in value of the designated hedged item. In the case of a qualifying cash flow hedge, changes in the value of the derivative instruments that are highly effective are recognized in accumulated other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value is recognized through earnings. Derivatives that are non-designated hedges are adjusted to fair value through earnings. Throughout 2006 and 2007, we had no derivatives designated as fair value hedges. On January 1, 2008, we derecognized all of our cash flow hedges.

Secondary Market Reserve. We sell most of the residential mortgage loans that we originate into the secondary mortgage market. When we sell mortgage loans we make customary representations and warranties to the purchasers about various characteristics of each loan, such as the manner of origination, the nature and extent of underwriting standards applied and the types of documentation being provided. Typically these representations and warranties are in place for the life of the loan. If a defect in the origination process is identified, we may be required to either repurchase the loan or indemnify the purchaser for losses it sustains on the loan. If there are no such defects, we have no liability to the purchaser for losses it may incur on such loan. We maintain a secondary market reserve to account for the expected credit losses related to loans we may be required to repurchase (or the indemnity payments we may have to make to purchasers). The secondary market reserve takes into account both our estimate of expected losses on loans sold during the current accounting period, as well as adjustments to our previous estimates of expected losses on loans sold. In each case, these estimates are based on our most recent data regarding loan repurchases, actual credit losses on repurchased loans and recovery history, among other factors. Increases to the secondary market reserve for current loan sales reduce our net gain on loan sales. Adjustments to our previous estimates are recorded as an increase or decrease in our other fees and charges.

Like our other critical accounting policies, our secondary market reserve is highly dependent on subjective and complex judgments and assumptions. We continue to enhance our estimation process and adjust our assumptions. Our assumptions are affected by factors both internal and external in nature. Internal factors include, among other things, level of loan sales, as well as to whom the loans are sold, improvements to technology in the underwriting process, expectation of credit loss on repurchased loans, expectation of loss from indemnification payments made to loan purchasers, the expectation of the mix between repurchased loans and indemnifications, our success rate at appealing repurchase demands and our ability to recover any losses from third parties. External factors that may affect our estimate includes, among other things, the overall economic condition in the housing market, the economic condition of borrowers, the political environment at investor agencies and the overall U.S. and world economy. Many of the factors are beyond our control and lend to judgments that are susceptible to change.

Results of Operations

Net Interest Income

2007. During 2007, we recognized $209.9 million in net interest income, which represented a decrease of 2.3% compared to the $214.9 million reported in 2006. Net interest income represented 64.2% of our total revenue in 2007 as compared to 51.5% in 2006. Net interest income is primarily the dollar value of the average yield we earn on the average balances of our interest-earning assets, less the dollar value of the average cost of funds we incur on the average balances of our interest-bearing liabilities. For the year ended December 31, 2007, we had an average balance of $15.0 billion of interest-earning assets, of which $12.4 billion were loans receivable. Interest income recorded on these loans is reduced by the amortization of net premiums and net deferred loan origination costs. Interest income for 2007 was $905.5 million, an increase of 13.1% from the $800.9 million recorded 2006. Offsetting the increase in interest income was an increase in our cost of funds. The average cost of interest-bearing liabilities increased 9.3%, from 4.32% during 2006 to 4.72% in 2007, while the average yield on interest-earning assets increased only 5.4%, from 5.74% during 2006 to 6.05% in 2007. As a result, our interest rate spread during 2007 was 1.33% at year-end. The compression of our interest rate spread during the year, combined with an increase in nonperforming assets caused our net interest margin for 2007 to decrease to 1.40% from 1.54% during 2006. Our net interest margin was also affected by the decline in our ratio of interest-earning assets to interest-bearing liabilities, from 103% in 2006 to 101% in 2007. The Bank recorded an interest rate margin of 1.50% in 2007, as compared to 1.63% in 2006.

2006. During 2006, we recognized $214.9 million in net interest income, which represented an decrease of 12.7% compared to the $246.3 million reported in 2005. Net interest income represented 51.5% of our total revenue in 2006 as compared to 60.7% in 2005. Net interest income is primarily the dollar value of the average yield we earn on the average balances of our interest-earning assets, less the dollar value of the average cost of funds we incur on the average balances of our interest-bearing liabilities. For the year ended December 31, 2006, we had an average balance of $14.0 billion of interest-earning assets, of which $12.2 billion were loans receivable. Interest income recorded on these loans is reduced by the amortization of net premiums and net deferred loan origination costs. Interest income for 2006 was $800.9 million, an increase of 13.0% from the $708.7 million recorded in 2005. Offsetting the increase in earning assets was an increase in our cost of funds. Our interest-earning assets are funded with deposits and other short-term liabilities, primarily borrowings from the FHLB and security repurchase agreements. Typically, there is a spread between the long-term rates we earn on these mortgage loans and the short-term rates we pay on our funding sources. During 2006, the spread between these interest rates narrowed as short-term rates increased. The average cost of interest-bearing liabilities increased 23.8% from 3.49%, during 2005 to 4.32% in 2006, while the average yield on interest-earning assets increased only 9.8%, from 5.23% during 2005 to 5.74% in 2006. As a result, our interest rate spread during 2006 was 1.42% at year-end. The compression of our interest rate spread during the year caused our net interest margin for 2006 to decrease to 1.54% from 1.82% during 2005. The adverse effect of the spread compression was offset in part by the increase in our ratio of interest-earning assets to interest-bearing liabilities, from 102% in 2005 to 103% in 2006. The Bank recorded an interest rate margin of 1.63% in 2006, as compared to 1.88% in 2005.

The following table presents interest income from average earning assets, expressed in dollars and yields, and interest expense on average interest-bearing liabilities, expressed in dollars and rates. Interest income from earning assets was reduced by $23.8 million, $28.3 million and $29.6 million of amortization of net premiums and net deferred loan origination costs in 2007, 2006 and 2005, respectively. Non-accruing loans were included in the average loans outstanding.

	For the Years Ended December 31,								
	2007			2006			2005		
	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate	Average Balance	Interest	Average Yield/ Rate
					(In thousands)				
Interest-Earning Assets:									
Loans receivable, net	$12,426,509	$769,485	6.19%	$12,166,346	$711,037	5.84%	$13,128,224	$688,791	5.25%
Mortgaged backed securities	1,237,989	59,960	4.84%	1,555,930	77,607	4.99%	370,405	19,019	5.13%
Other	1,299,544	76,064	5.85%	229,117	12,222	5.33%	51,737	853	1.65%
Total interest-earning assets	14,964,042	905,509	6.05%	13,951,393	$800,866	5.74%	13,550,366	$708,663	5.23%
Other assets	1,226,178			1,330,755			1,240,143		
Total assets	$16,190,220			$15,282,148			$14,790,509		
Interest-Bearing Liabilities:									
Deposits	$ 7,716,896	$357,430	4.63%	$ 8,030,276	$331,516	4.13%	$ 7,971,506	$253,292	3.18%
FHLB advances	5,847,888	271,443	4.64%	4,270,660	187,756	4.40%	4,742,079	182,377	3.85%
Security repurchase agreements	954,772	51,458	5.39%	1,028,916	52,389	5.09%	187,585	7,953	4.24%
Other	225,827	15,300	6.78%	232,149	14,258	6.14%	347,224	18,771	5.41%
Total interest-bearing liabilities	14,745,383	$695,631	4.72%	13,562,001	$585,919	4.32%	13,248,394	$462,393	3.49%
Other liabilities	681,879			921,655			792,781		
Stockholders' equity	762,958			798,492			749,334		
Total liabilities and stockholders equity	$16,190,220			$15,282,148			$14,790,509		
Net interest-earning assets	$ 218,659			$ 389,392			$ 301,972		
Net interest income		$209,878			$214,947			$246,270	
Interest rate spread(1)			1.33%			1.42%			1.74%
Net interest margin(2)			1.40%			1.54%			1.82%
Ratio of average interest-earning assets to interest-bearing liabilities			101%			103%			102%

(1) Interest rate spread is the difference between rates of interest earned on interest-earning assets and rates of interest paid on interest-bearing liabilities.

(2) Net interest margin is net interest income divided by average interest-earning assets.

Rate/Volume Analysis

The following table presents the dollar amount of changes in interest income and interest expense for the components of interest earning assets and interest-bearing liabilities that are presented in the preceding table. The table below distinguishes between the changes related to average outstanding balances (changes in volume while holding the initial rate constant) and the changes related to average interest rates (changes in average rates while holding the initial balance constant). Changes attributable to both a change in volume and a change in rates were included as changes in rate.

	For the Years Ended December 31,					
	2007 Versus 2006 Increase (Decrease) Due to:			2006 Versus 2005 Increase (Decrease) Due to:		
	Rate	Volume	Total	Rate	Volume	Total
	(Dollars in millions)					
Interest-Earning Assets:						
Loans receivable, net	$43.4	$ 15.2	$ 58.6	$ 72.7	$(50.5)	$ 22.2
Mortgage-backed securities	(1.8)	(15.9)	(17.7)	(2.2)	60.8	58.6
Other	6.7	57.0	63.7	8.4	2.9	11.3
Total	$48.3	$ 56.3	$104.6	$ 78.9	$ 13.2	$ 92.1
Interest- Bearing Liabilities:						
Total deposits	$38.9	$(12.9)	$ 26.0	$ 76.4	$ 1.8	$ 78.2
FHLB advances	14.3	69.4	83.7	23.5	(18.2)	5.3
Security repurchase agreements	2.8	(3.8)	(1.0)	8.8	35.6	44.4
Other	1.4	(0.4)	1.0	1.7	(6.2)	(4.5)
Total	$57.4	$ 52.3	$109.7	$110.4	$ 13.0	$123.4
Change in net interest income	$ (9.1)	$ 4.0	$ (5.1)	$ (31.5)	$ 0.2	$ (31.3)

Provision for Loan Losses

During 2007, we recorded a provision for loan losses of $88.3 million as compared to $25.4 million recorded during 2006 and $18.9 million recorded in 2005. The provisions reflect our estimates to maintain the allowance for loan losses at a level to cover probable losses in the portfolio for each of the respective periods.

The increase in the provision during 2007 as compared to 2006, which increased the allowance for loan losses to $104.0 million at December 31, 2007 from $45.8 million at December 31, 2006, reflects the increase in net charge-offs both as a dollar amount and as a percentage of the loans held for investment, and it also reflects the increase in overall loan delinquencies (i.e., loans at least 30 days past due) in 2007. Net charge-offs in 2007 totaled $30.1 million as compared to $18.8 million in 2006, resulting from increased charge-offs of home equity and first and second residential mortgage loans and commercial real estate loans. As a percentage of the average loans held for investment, net charge-offs in 2007 increased to 0.38% from 0.20% in 2006. At the same time, overall loan delinquencies increased to 4.03% of total loans held for investment at December 31, 2007 from 1.34% at December 31, 2006. Total delinquent loans increased to $327.4 million at December 31, 2007 as compared to $119.4 million at December 31, 2006. In 2007, the increase in delinquencies impacted all categories of loans within the held for investment portfolio. The overall delinquency rate on residential mortgage loans increased to 3.74% at December 31, 2007 from 1.59% at December 31, 2006. The overall delinquency rate on commercial real estate loans increased to 6.13% at December 31, 2007 from 0.66% at December 31, 2006.

The increase in the provision during 2006 as compared to 2005, which increased the allowance for loan losses to $45.8 million at December 31, 2006 from $39.1 million at December 31, 2005, reflects the increase in net charge-offs both as a dollar amount and as a percentage of the loans held for investment, and it also reflects the increase in overall loan delinquencies (i.e., loans at least 30 days past due) in 2006. Net charge-offs in 2006 totaled $18.8 million as compared to $18.1 million in 2005, reflecting increased charge-offs of home equity and second mortgage loans and of overdrafts from checking accounts. As a percentage of the average loans held for investment, net charge-offs in 2006 increased to 0.20% from 0.16% in 2005. At the same time, overall loan delinquencies increased to 1.34% of total loans held for investment at December 31, 2006 from 1.10% at December 31, 2005, Total delinquent loans increased to $119.4 million in 2006 as compared to $115.9 million in 2005. The increase in delinquencies related primarily to residential mortgage loans, increasing to 1.59% at December 31, 2006 from 1.16% at December 31, 2005, as well as slight increases in delinquencies of home equity and second mortgage loans.

See the section captioned "Allowance for Loan Losses" in this discussion for further analysis of the provision for loan losses.

Non-Interest Income

Our non-interest income consists of (i) loan fees and charges, (ii) deposit fees and charges, (iii) loan administration, (iv) net gain on loan sales, (v) net gain on sales of MSRs, (vi) net loss on securities available for sale, (vii) loss on trading securities, and (viii) other fees and charges. Our total non-interest income equaled $117.1 million during 2007, which was a 42.1% decrease from the $202.2 million of non-interest income that we earned in 2006. The primary reason for the decrease was the decrease in 2007 of net gains from sales of MSRs.

Loan Fees and Charges. Both our home lending operation and banking operation earn loan origination fees and collect other charges in connection with originating residential mortgages and other types of loans. In each period, we recorded fee income net of any fees deferred for the purposes of complying with Statement of Financial Accounting Standard ("SFAS") 91, *"Accounting for Non-Refundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases."* During 2007, we recorded gross loan fees and charges of $78.0 million, an increase of $27.1 million from the $50.9 million recorded in 2006 and the $71.6 million recorded in 2005. The increase in loan fees and charges resulted from an increase in the volume of loans originated during 2007 compared to 2006.

In accordance with SFAS 91, loan origination fees are capitalized and added as an adjustment to the basis of the individual loans originated. These fees are accreted into income as an adjustment to the loan yield over the life of the loan or when the loan is sold. During 2007, we deferred $76.5 million of fee revenue in accordance with SFAS 91, compared to $43.4 million and $59.0 million, respectively, in 2006 and 2005. This increase results from a 32.1% increase in total loan production during 2007 over 2006, as well as, significant enhancements to our systems and processes with respect to the capture of direct loan fees and charges for all types of our loans. These enhancements have been in process since 2006 but were completed in 2007. We began the enhancement process as a result of our continued expansion of our lending products, particularly commercial real estate loans, second mortgage and home equity lines-of-credit.

Deposit Fees and Charges. Our banking operation collects deposit fees and other charges such as fees for non-sufficient funds checks, cashier check fees, ATM fees, overdraft protection, and other account fees for services we provide to our banking customers. The amount of these fees tends to increase as a function of the growth in our deposit base. Total deposit fees and charges increased 10.0% during 2007 to $23.0 million compared to $20.9 million during 2006 and $16.9 million during 2005. During that time, total customer accounts grew from 277,900 at January 1, 2006 to 293,236 at December 31, 2007.

Loan Administration. When our home lending operation sells mortgage loans in the secondary market, it usually retains the right to continue to service these loans and earn a servicing fee. When an underlying loan is prepaid or refinanced, the mortgage servicing right for that loan is fully amortized as no further fees will be earned for servicing that loan. During periods of falling interest rates, prepayments and refinancings generally increase and, unless we provide replacement loans, it will usually result in a reduction in loan servicing fees and increase amortization recorded on the MSR portfolio.

Our loan administration fees and MSR amortization can fluctuate significantly. Such fees are affected by the size of our loans serviced for others portfolio, which is affected by sales of MSRs, subservicing fees, late fees and ancillary income and past due status of serviced loans. When loans serviced for others become ninety days or more past due we cease accruing servicing fees on such loans. Amortization of MSRs can be affected by sales of MSRs and changes in interest rates that cause changes in prepayments of the underlying loans. Changes in loan administration fees and changes in amortization of MSRs will not necessarily occur in proportion.

During 2007, the volume of loans serviced for others averaged $23.4 billion, which represented a 15.3% increase from the $20.3 billion serviced during 2006. During 2007, we recorded $91.1 million in servicing fee revenue. The fee revenue recorded in 2007 was offset by $78.4 million of MSR amortization. During 2006, we recorded $82.6 million in servicing fee revenue which was offset by $69.6 million of MSR amortization. During 2007, the amount of loan principal payments and payoffs received on serviced loans equaled $3.2 billion, a 5.9% decrease from the 2006 total of $3.4 billion. The decrease was primarily attributable to a continuing decline in mortgage loan refinancing in 2007 due to, among other things, the global liquidity crisis and the decline in housing values throughout the United States.

Net Gain on Loan Sales. Our home lending operation records the transaction fee income it generates from the origination, securitization and sale of mortgage loans in the secondary market. The amount of net gain on loan sales recognized is a function of the volume of mortgage loans sold and the gain on sale spread achieved, net of related selling expenses. Net gain on loan sales is also increased or decreased by any mark to market pricing adjustments on loan commitments and forward sales commitments in accordance with SFAS No. 133, *"Accounting for Derivative Instruments"* ("SFAS 133"), increases to the secondary market reserve related to loans sold during the period, and related administrative expenses. The volatility in the gain on sale spread is attributable to market pricing, which changes with demand and the general level of interest rates. Generally, we are able to sell loans into the secondary market at a higher margin during periods of low or decreasing interest rates. Typically, as the volume of acquirable loans increases in a lower or falling interest rate environment, we are able to pay less to acquire loans and are then able to achieve higher spreads on the eventual sale of the acquired loans. In contrast, when interest rates rise, the volume of acquirable loans decreases and therefore we may need to pay more in the acquisition phase, thus decreasing our net gain achievable. Prior to the global liquidity crisis that arose in the third quarter of 2007, our net gain was also affected by declining spreads available from securities we sell that are guaranteed by Fannie Mae and Freddie Mac and by an over-capacity in the mortgage business that had placed continuing downward pressure on loan pricing opportunities for conventional residential mortgage products. In the latter part of 2007, these trends began to reverse as competitors left the mortgage industry and spreads widened.

The following table provides information on our net gain on loan sales reported in our consolidated financial statements to our loans sold within the period (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
Net gain on loan sales	$ 59,030	$ 42,381	$ 63,580
Loans sold and securitized	$24,255,114	$16,370,925	$23,451,430
Spread achieved	0.24%	0.26%	0.27%

2007. Net gain on loan sales totaled $59.0 million during 2007, a 39.2% increase from the $42.4 million realized during 2006. During 2007, the volume of loans sold and securitized totaled $24.3 billion, a 48.0% increase from the $16.4 billion of loan sales in 2006. Our calculation of net gain on loan sales reflects changes in amounts related to SFAS 133 pricing adjustments, lower of cost or market adjustments for loans transferred to held for investment and provisions to our secondary market reserve. Changes in amounts related to SFAS 133 pricing adjustments amounted to $(4.4) million and $(4.5) million for the years ended December 31, 2007 and 2006, respectively. Lower of cost or market adjustments for loans transferred to held for investment amounted to $2.7 million and $2.0 million for the years ended December 31, 2007 and 2006, respectively. Provisions to our secondary market reserve amounted to $9.5 million and $5.9 million, for the years ended December 31, 2007 and 2006, respectively. Also included in our net gain on loan sales are the capitalized value of our MSR's, which totaled $346.4 million and $223.9 million for the years ended December 31, 2007 and 2006, respectively. We also reduced our net gain on loan sales by the amount of credit losses incurred on our available for sale portfolio, and such losses totaled $3.6 million in 2007 and $1.4 million in 2006.

2006. Net gain on loan sales totaled $42.4 million during 2006, a 33.3% decrease from the $63.6 million realized during 2005. During 2006, the volume of loans sold and securitized totaled $16.4 billion, a 30.2% decrease from the $23.5 billion of loan sales in 2005. Our calculation of net gain on loan sales reflects changes in amounts related to SFAS 133 pricing adjustments, lower of cost or market adjustments for loans transferred to held for investment and provisions to our secondary market reserve. Changes in amounts related to SFAS 133 pricing adjustments amounted to $(4.4) million and $2.9 million for the years ended December 31, 2006 and 2005, respectively. Lower of cost or market adjustments for loans transferred to held for investment amounted to $2.0 million and $87,000 for the years ended December 31, 2006 and 2005, respectively. Provisions to our secondary market reserve amounted to $5.9 million and $5.3 million, for the years ended December 31, 2006 and 2005, respectively. Also included in our net gain on loan sales is the capitalized value of our MSR's, which totaled $223.9 million and $329.0 million for the years ended December 31, 2006 and 2005, respectively.

Net Gain on Sales of Mortgage Servicing Rights. As part of our business model, our home lending operation occasionally sells MSRs in transactions separate from the sale of the underlying loans. At the time of the MSR sale, we record a gain or loss based on the selling price of the MSRs less our carrying value and transaction costs. Accordingly, the amount of net gains on MSR sales depends upon the gain on sale spread and the volume of MSRs sold. The spread is attributable to market pricing, which changes with demand, and the general level of interest rates. In general, if an MSR is sold on a "flow basis" shortly after it is acquired, little or no gain will be realized on the sale. MSRs created in a lower interest rate environment generally will have a higher market value because the underlying loan is less likely to be prepaid. Conversely, an MSR created in a higher interest rate environment will generally sell at a market price below the original fair value recorded because of the increased likelihood of prepayment of the underlying loans, resulting in a loss.

2007. During 2007, the net gain on the sale of MSRs totaled $5.9 million compared to a net gain of $92.6 million in 2006. The $86.7 million decrease in net gain on the sale of MSRs is primarily due to a significant decrease in the volume of MSRs sold in 2007. We sold $1.5 billion in loans on a servicing released basis and $2.03 billion in bulk servicing sales in 2007.

2006. During 2006, the net gain on the sale of MSRs totaled $92.6 million compared to a net gain of $18.2 million in 2005. The $74.4 million increase in net gain on the sale of MSRs is primarily due to a significant increase in the volume of MSRs sold in 2006. Throughout 2006, we believed that the market price accurately reflected the MSR value. As a result, we sold more MSRs in 2006 than prior periods. We sold $2.3 billion in loans on a servicing released basis and $25.2 billion in bulk servicing sales in 2006.

Net Loss on Securities Available for Sale. Securities classified as available for sale are comprised of residual interests from private-label securitizations and mortgage-backed and collateralized mortgage obligation securities.

2007. During 2007, we recognized a net loss on securities available for sale of $16.7 million. The net loss included a gain of $4.5 million on sales of securities available for sale, offset by an impairment of non-agency AAA rated securities available for sale of $2.8 million and by an impairment of non-investment grade residual assets of $18.4 million.

The $4.5 million gain on sale of securities available for sale resulted from the sale of AAA-rated agency and non-agency mortgage-backed securities with a principal balance of $538.4 million.

The impairment of non-agency AAA rated securities available for sale of $2.8 million was as a result of management's determination that the loss in the fair value of a specific mortgage-backed security was other-than-temporary. Consequently, the $2.8 million was charged to operations rather than recorded in other comprehensive income (loss). See Note — 4 to our Consolidated Financial Statements included in Part II, Item 8, Financial Statements and Supplemental Data, herein.

During 2007, we recognized an $18.4 million other-than-temporary impairment on our residual interests that arose from private-label securitizations completed in 2006 and 2005. Although the residual interests are accounted for as available for sale assets, we determined that the impairment was other-than-temporary and therefore a loss should be recorded.

The $18.4 million in impairment charges on our residual interests resulted from unfavorable trends in the mortgage industry, benchmarking procedures applied against available industry data and our own experience that resulted in adjusting the critical assumptions utilized in valuing such securities relating to prepayment speeds, expected credit losses and the discount rate. The principal changes to our assumptions that caused the decline in fair value of these residuals were our increase in credit loss estimates and the discount rate. During 2007, we increased the credit loss estimates from 1.25% on our home equity lines of credit residual assets to 2.88% for the 2005 securitization and 4.99% for the 2006 securitization. We increased the credit loss estimates for our 2006 second mortgage securitization from 1.50% to 2.86%. Further, we increased the discount rate assumption from 15% to 20% during 2007 for all available-for-sale residual assets.

2006. The $6.1 million in impairment charges on our residual interest in 2006 resulted from changes in the interest rate environment, benchmarking procedures applied against updated industry data and third party valuation data that resulted in adjusting the critical prepayment speed assumption utilized in valuing such security. Specifically, we completed a private securitization of home equity lines of credit in the fourth quarter of 2005. In determining the appropriate assumptions to model the transaction, we utilized our recent history of similar products, available industry information and advice from third party consultants experienced in securitizations. At the same time, we had observed prepayment speeds in the 30%-35% CPR range for our portfolio, which was consistent with the available industry data. After consulting with our advisors, we utilized a 40% CPR assumption in our modeling in order to reflect our belief that there would be only a modest increase in the prepayment speeds in the near term due to our expectations of interest rate movements and the possibility of an inverted yield curve. As short-term interest rates increased throughout the fourth quarter of 2005 and the first quarter of 2006 and the yield curve flattened, the prepayment speed of the portfolio increased at a much higher rate than anticipated. We attributed this to fixed rate loans that became available at lower rates than the adjustable-rate home equity lines of credit ("HELOC") loans in the securitization pool. We also noted that this increased prepayment speed with HELOCs was occurring industry-wide. The appropriateness of adjusting the model's prepayment speed upward was validated with both a third party valuation firm and with our own backtesting procedures. Based on this information, we adjusted our cash flow model to incorporate our updated prepayment speed during the first quarter of 2006. At March 31, 2006, a significant deterioration of the residual asset was determined to have occurred. We further analyzed the result and determined that approximately $3.5 million of the deterioration was other than temporary. An additional amount of the deterioration was deemed to be temporary and recorded as a portion of other comprehensive income. This was based on our belief, following further discussions with our advisors, that prepayment speeds would moderate during the year as the portfolio seasoned. However, as the yield curve continued to flatten and even invert during the third and fourth quarters of 2006, prepayment speeds not only failed to moderate, but actually accelerated. Additionally, based on our analysis, we did not believe that the inverted yield curve would only be a short-term phenomenon. Based on these factors and our cash flow models, we determined that additional permanent impairment had taken place. Such amounts were recorded as identified and resulted in the $6.1 million in impairment charges for 2006.

Loss on Trading Securities. Securities classified as trading are comprised of residual interests from the private-label securitization completed in March 2007, with the secondary closing in June 2007. Loss on securities classified as trading is the result of a reduction in the estimated fair value of the security with the related loss recorded in the statement of operations.

2007. During 2007, we recognized $6.8 of losses on our residual interests from the private-label securitization, completed in March 2007. The loss is the result of unfavorable trends in the mortgage industry, benchmarking procedures applied against available industry data and our own experience that resulted in adjusting the critical assumptions utilized in valuing such security relating to prepayment speeds, loss expectations and the discount rate. The principal causes for the loss on our residual asset was due to our increase in the credit loss estimate from 1.50% to 3.28% and the increase in the discount rate from 15% to 20% at December 31, 2007. We had no trading assets during 2006 or prior.

Other Fees and Charges. Other fees and charges include certain miscellaneous fees, including dividends received on FHLB stock and income generated by our subsidiaries Flagstar Reinsurance Company (formerly Flagstar Credit, Inc.) and Douglas Insurance Agency, Inc.

During 2007, we recorded $15.0 million in dividends on an average outstanding balance of FHLB stock of $328.3 million as compared to $14.7 million and $11.1 million in dividends on an average balance of FHLB stock outstanding of $284.2 million and $264.2 million in 2006 and 2005, respectively. During 2007, Flagstar Reinsurance Company earned fees of $5.0 million versus $4.8 million and $4.9 million in 2006 and 2005, respectively. The amount of fees earned by Flagstar Reinsurance Company varies with the volume of loans that were insured during the respective periods. In addition, during 2007, we recorded in other fees and charges $9.7 million related to our successful efforts to mitigate losses incurred in connection with a fraud discovered in 2004 relating to a series of warehouse loans.

Non-Interest Expense

The following table sets forth detailed information regarding our non-interest expenses during the past three years.

NON-INTEREST EXPENSES

	For the Years Ended December 31,		
	2007	2006	2005
	(Dollars in thousands)		
Compensation and benefits	$179,417	$157,751	$ 150,738
Commissions	83,047	74,208	87,746
Occupancy and equipment	69,218	70,319	69,121
Advertising	10,334	9,394	7,550
FDIC assessments	4,354	1,115	1,146
Communication	6,317	6,190	7,181
Other taxes	(1,756)	320	10,127
Other	41,497	49,824	46,362
Total	392,428	369,121	379,971
Less: capitalized direct costs of loan closings, in accordance with SFAS 91	(94,918)	(93,484)	(117,084)
Total, net	$297,510	$275,637	$ 262,887
Efficiency ratio(1)	91.0%	66.1%	64.8%

(1) Total operating and administrative expenses divided by the sum of net interest income and non-interest income

2007. Non-interest expenses, before the capitalization of direct costs of loan closings, totaled $392.4 million in 2007 compared to $369.1 million in 2006. The 6.3% increase in non-interest expense in 2007 was largely due to an increase in compensation and benefits, higher commissions resulting from an increase in the volume of loan originations in our home lending operations, and higher FDIC assessments resulting from changes initiated by the FDIC. During 2007, we opened 13 banking centers, which brings the banking center network total to 164. As we increase the size of the banking center network, we expect that the operating expenses associated with the banking center network will continue to increase.

Our gross compensation and benefit expense, before the capitalization of direct costs of loan closings, totaled $179.4 million. The 13.7% increase from 2006 is primarily attributable to normal salary increases and the employees hired at the new banking centers and, to a lesser extent, salaries paid to home loan center employees hired during the third quarter. Our full-time equivalent ("FTE") salaried employees increased by 589 to 3,083 at December 31, 2007, reflecting employees hired for new banking centers, home loan center employees during the third quarter 2007, and an increase in account executives hired for the wholesale loan business. Commission expense, which is a variable cost associated with loan production, totaled $83.0 million, equal to 31 basis points (0.31%) of total loan production in 2007. Occupancy and equipment totaled $69.2 million during 2007, which reflects the continuing expansion of our deposit banking center network, offset in part by the closing of various non-profitable home loan centers. Advertising expense, which totaled $10.3 million at December 31, 2007, increased $0.9 million, or 10.0%, from the $9.4 million reported in 2006. Our FDIC assessment was $4.4 million at December 31, 2007 as compared to $1.1 million at 2006. We paid $6.3 million in communication expense for the year-ended December 31, 2007. These expenses typically include telephone, fax and other types of electronic communication. The increase in communication expenses is reflective of an increase in home loan centers. We pay taxes in the various states and local communities in which we are located and/or do business. For the year ended December 31, 2007 our state and local taxes totaled a tax benefit of $(1.8) million, a decrease of $2.1 million. Other expense totaled $41.5 million during 2007. The fluctuation in other expenses is reflective of the expansion undertaken in our banking operation as well as our home lending operation as we continue to increase our national presence offset in part by the closing of non-profitable home loan centers, and general cost containment efforts.

2006. Non-interest expenses, before the capitalization of direct costs of loan closings, totaled $369.1 million in 2006 compared to $380.0 million in 2005. The 2.9% decrease in non-interest expense in 2006 was largely due to lower commissions resulting from a decrease in the volume of loan originations in our home lending operations and from our general cost containment efforts. Offsetting the savings in our home lending operation were certain expenses associated with the increase in the number of banking centers operated by our banking operation. During 2006, we opened 14 banking centers, which brought the banking center network total to 151.

Our gross compensation and benefit expense, before the capitalization of direct costs of loan closings, totaled $157.8 million at December 31, 2006. The 4.7% increase from 2005 is primarily attributable to normal salary increases and the employees hired at the new banking centers. Our FTE salaried employees increased by 105 to 2,510 at December 31, 2006. Commission expense, which is a variable cost associated with loan production, totaled $74.2 million, equal to 37 basis points (0.37%) of total loan production in 2006. Occupancy and equipment totaled $70.3 million during 2006, which reflects the continuing expansion of our deposit banking center network, offset in part by the closing of various non- profitable home loan centers. Advertising expense, which totaled $9.4 million at December 31, 2006, increased $1.8 million, or 23.7%, from the $7.6 million reported in 2005. Our FDIC assessment remained the same at $1.1 million as compared to 2005. We paid $6.2 million in communication expense for the year-ended December 31, 2006. These expenses typically include telephone, fax and other types of electronic communication. The decrease in communication expenses is reflective of fewer home loan centers. We pay taxes in the various states and local communities in which we are located and/or do business. For the year ended December 31, 2006 our state and local taxes totaled $0.3 million, a decrease of $9.8 million, which is the result of a restructuring of our corporate operations that better aligned our core functions in separate entities. Other expense totaled $49.8 million during 2006. The fluctuation in other expenses is reflective of the varied levels of loan production, the expansion undertaken in our banking operation offset by the closing of the non-profitable home loan centers and the dismissal of our lawsuit against an insurance company in a coverage dispute that resulted in a charge in November 2006, of $8.7 million, before taxes.

Capitalization of Loan Fees and Costs

Loan origination fees and costs are capitalized and recorded as an adjustment to the basis of the individual loans originated. These fees and costs are amortized or accreted into income as an adjustment to the loan yield over the life of the loan or expensed when the loan is sold. Accordingly, during 2007, we deferred $94.9 million of gross loan origination costs, while during 2006 and 2005 the deferred expenses totaled $93.5 million and $117.1 million, respectively. These costs have not been offset by the revenue deferred for SFAS 91 purposes. During the year to date in 2007 and the years 2006 and 2005, we deferred $76.5 million, $43.4 million, and $59.0 million in qualifying loan fee revenue, respectively. For further information, see "Loan Fees and Charges," above.

On a per loan basis, the cost deferrals totaled $775, $992, and $816 during 2007, 2006, and 2005, respectively. Net of deferred fee income, the cost deferred per loan totaled $151, $531, and $405 for years

2007, 2006, and 2005, respectively. On a per loan basis, the cost deferrals for commissions totaled $678, $788, and $566 during 2007, 2006, and 2005, respectively.

(Benefit) Provision for Federal Income Taxes

For the year ended December 31, 2007, our benefit for federal income taxes as a percentage of pretax loss was 33.3% compared to provisions on pretax earnings of 35.2% in 2006 and 35.6% in 2005. For each period, the (benefit) provision for federal income taxes varies from statutory rates primarily because of certain non-deductible corporate expenses. Refer to Note 16 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data herein for further discussion of our federal income taxes.

Analysis of Items on Statement of Financial Condition

Securities Classified as Trading. Securities classified as trading are comprised of residual interests from the private-label securitization closed in March 2007 with a secondary closing in June 2007. The residual interest in this securitization was $13.7 million at December 31, 2007. In accordance with SFAS 155, *"Accounting for Certain Hybrid Instruments,"* management has elected to initially and subsequently measure this residual interest from the March 2007 securitization, and subsequent securitizations, at fair value. This does not affect the classification of the residuals from prior securitizations. Subsequent changes to fair value are recorded in operations in the period of the change. See Note 4 in the "Notes to Consolidated Financial Statements," in Item 8. Financial Statements, herein.

Securities Classified as Available for Sale. Securities classified as available for sale, which are comprised of mortgage-backed securities, collateralized mortgage obligations and residual interests from securitizations of mortgage loan products, increased from $617.5 million at December 31, 2006, to $1.3 billion at December 31, 2007. At December 31, 2007, approximately $570.0 million of these securities classified as available for sale were pledged as collateral under security repurchase agreements. See Note 4 in the "Notes to Consolidated Financial Statements," in Item 8. Financial Statements herein.

Mortgage-backed Securities Held to Maturity. Mortgage-backed securities held to maturity decreased from $1.6 billion at December 31, 2006 to $1.3 billion at December 31, 2007. The decrease was attributable to the repayment of principal and the reclassification, in March 2007, of $321.1 million securities associated with the guaranteed mortgage securitization of fixed second mortgage loans completed in April 2006 to available for sale. At December 31, 2007, approximately $107.6 million of mortgage-backed securities were pledged as collateral under security repurchase agreements and swap agreements as compared to $1.0 billion at December 31, 2006. See Note 4 in the "Notes to Consolidated Financial Statements," in Item 8. Financial Statements herein.

Other Investments. Our investment portfolio increased from $24.0 million at December 31, 2006 to $26.8 million at December 31, 2007. Investment securities consist of contractually required collateral, regulatory required collateral, and investments made by our non-bank subsidiaries.

Loans Available for Sale. We sell a majority of the mortgage loans we produce into the secondary market on a whole loan basis or by securitizing the loans into mortgage-backed securities. At December 31, 2007, we held loans available for sale of $3.5 billion, which was an increase of $0.3 billion from $3.2 billion held at December 31, 2006. Our loan production is typically inversely related to the level of long-term interest rates. As long-term rates decrease, we tend to originate an increasing number of mortgage loans. A significant amount of the loan origination activity during periods of falling interest rates is derived from refinancing of existing mortgage loans. Conversely, during periods of increasing long-term rates, loan originations tend to decrease.

The following table shows the activity in our portfolio of loans available for sale during the past five years:

LOANS AVAILABLE FOR SALE ACTIVITY SCHEDULE

	For the Years Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Balance, beginning of year	$ 3,188,795	$ 1,773,394	$ 1,506,311	$ 2,759,551	$ 3,302,212
Loans originated, net	26,054,106	18,057,340	25,202,205	31,943,915	55,866,218
Loans sold servicing retained, net	(22,965,827)	(13,974,425)	(21,608,937)	(27,749,138)	(49,681,387)
Loans sold servicing released, net	(1,524,506)	(2,395,465)	(1,855,700)	(1,352,789)	(2,461,326)
Loan amortization/ prepayments	(541,956)	(1,246,419)	(1,040,315)	(1,798,137)	(1,652,811)
Loans transferred from (to) various loan portfolios, net	(699,302)	974,370	(430,170)	(2,297,091)	(2,613,355)
Balance, end of year	$ 3,511,310	$ 3,188,795	$ 1,733,394	$ 1,506,311	$ 2,759,551

Loans Held for Investment. Our largest category of earning assets consists of our loans held for investment portfolio. Loans held for investment consists of residential mortgage loans that we do not hold for resale (usually shorter duration and adjustable rate loans and second mortgages), other consumer loans, commercial real estate loans, construction loans, warehouse loans to other mortgage lenders, and various types of commercial loans such as business lines of credit, working capital loans and equipment loans. Loans held for investment decreased from $8.9 billion in December 2006, to $8.0 billion in December 2007. Mortgage loans held for investment decreased $387.8 million to $5.8 billion, second mortgage loans decreased $658.6 million to $56.5 million, commercial real estate loans increased $240.3 million to $1.5 billion and consumer loans decreased $58.4 million to $281.7 million. For information relating to the concentration of credit of our loans held for investment, see Note 22 in the "Notes to the Consolidated Financial Statements," in Item 8. Financial Statement, herein.

The following table sets forth a breakdown of our loans held for investment portfolio at December 31, 2007:

LOANS HELD FOR INVESTMENT, BY RATE

	Fixed Rate	Adjustable Rate	Total
	(Dollars in thousands)		
Mortgage loans	$1,019,318	$4,804,634	$5,823,952
Second mortgage loans	52,071	4,445	56,516
Commercial real estate loans	693,545	848,559	1,542,104
Construction loans	21,920	68,481	90,401
Warehouse lending	—	316,719	316,719
Consumer	100,845	180,901	281,746
Non-real estate commercial loans	8,916	14,043	22,959
Total	$1,896,615	$6,237,782	$8,134,397

The two tables below provide detail for the activity and the balance in our loans held for investment portfolio over the past five years.

LOANS HELD FOR INVESTMENT

	At December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Mortgage loans	$5,823,952	$6,211,765	$ 8,248,897	$ 8,693,768	$5,478,200
Second mortgage loans	56,516	715,154	700,492	196,518	141,010
Commercial real estate loans	1,542,104	1,301,819	995,411	751,730	549,456
Construction loans	90,401	64,528	65,646	67,640	58,323
Warehouse lending	316,719	291,656	146,694	249,291	346,780
Consumer loans	281,746	340,157	410,920	591,107	259,656
Non-real estate commercial loans	22,959	14,606	8,411	9,100	8,638
Total loans held for investment portfolio	8,134,397	8,939,685	10,576,471	10,559,154	6,842,063
Allowance for loan losses	(104,000)	(45,779)	(39,140)	(38,318)	(37,828)
Total loans held for investment portfolio, net	$8,030,397	$8,893,906	$10,537,331	$10,520,836	$6,804,235

LOANS HELD FOR INVESTMENT PORTFOLIO ACTIVITY SCHEDULE

	For the Years Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Balance, beginning of year	$ 8,939,685	$10,576,471	$10,559,154	$ 6,842,063	$ 3,986,751
Loans originated	996,702	2,406,068	5,101,206	4,840,028	1,901,105
Change in lines of credit	153,604	(244,666)	186,041	(189,696)	1,267,338
Loans transferred (to) from various portfolios, net	383,403	(1,018,040)	400,475	2,297,091	2,613,355
Loan amortization/prepayments	(2,223,258)	(2,696,441)	(5,622,989)	(3,190,640)	(2,890,680)
Loans transferred to repossessed assets	(115,739)	(83,707)	(47,416)	(39,692)	(35,806)
Balance, end of year	$ 8,134,397	$ 8,939,685	$10,576,471	$10,559,154	$ 6,842,063

Quality of Earning Assets

The following table sets forth certain information about our non-performing assets as of the end of the last five years.

NON-PERFORMING LOANS

	At December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Non-accrual loans	$197,149	$ 57,071	$ 64,466	$ 57,026	$ 58,334
Repurchased non-performing assets, net	9,776	22,096	34,777	35,013	11,956
Real estate and other repossessed assets, net	109,274	80,995	47,724	37,823	36,778
Total non-performing assets, net	$316,199	$160,162	$146,967	$129,862	$107,068
Ratio of non-performing assets to total assets	2.00%	1.03%	0.98%	0.99%	1.01%
Ratio of non-accrual loans to loans held for investment	2.42%	0.64%	0.61%	0.54%	0.85%
Ratio of allowance to non-accrual loans	52.75%	80.21%	60.71%	67.19%	64.85%
Ratio of allowance to loans held for investment	1.28%	0.51%	0.37%	0.36%	0.55%
Ratio of net charge-offs to average loans held for investment	0.35%	0.20%	0.16%	0.16%	0.35%

Delinquent Loans. Loans are considered to be delinquent when any payment of principal or interest is past due. While it is the goal of management to work out a satisfactory repayment schedule with a delinquent borrower, we will undertake foreclosure proceedings if the delinquency is not satisfactorily resolved. Our procedures regarding delinquent loans are designed to assist borrowers in meeting their contractual obligations. We customarily mail several notices of past due payments to the borrower within 30 days after the due date, and late charges are assessed in accordance with certain parameters. Our collection department makes telephone or personal contact with borrowers after a 30-day delinquency. In certain cases, we recommend that the borrower seek credit-counseling assistance and may grant forbearance if it is determined that the borrower is likely to correct a loan delinquency within a reasonable period of time. We cease the accrual of interest on loans that we classify as "non-performing" because they are more than 90 days delinquent. Such interest is recognized as income only when it is actually collected. At December 31, 2007, we had $327.4 million in loans that were determined to be delinquent. Of those delinquent loans, $197.1 million of loans were non-performing, of which $139.1 million, or 70.5%, were single-family residential mortgage loans.

The following table sets forth information regarding delinquent loans as of the end of the last three years (dollars in thousands):

DELINQUENT LOANS

	At December 31,		
Days Delinquent	2007	2006	2005
30	$ 59,811	$ 40,140	$ 30,972
60	70,450	22,163	20,456
90	197,149	57,071	64,466
Total	$327,410	$119,374	$115,894

We currently calculate our delinquent loans using a method required by the Office of Thrift Supervision, when we prepare regulatory reports that we submit to the OTS each quarter. This method also called the "OTS Method," considers a loan to be delinquent if no payment is received after the first day of the month following the month of the missed payment. Other companies with mortgage banking operations similar to ours usually use the Mortgage Bankers Association Method ("MBA Method") which considers a loan to be delinquent if payment is not received by the end of the month of the missed payment. The key difference between the two methods is that a loan considered "delinquent" under the MBA Method would not be considered "delinquent" under the OTS Method for another 30 days. Under the MBA Method of calculating delinquent loans, 30 day delinquencies equaled $150.9 million, 60 day delinquencies equaled $59.8 million and 90 day delinquencies equaled $267.6 million at December 31, 2007. Total delinquent loans under the MBA Method total $478.3 million or 5.88% of loans held for investment at December 31, 2007. By comparison, delinquent loans at year-end 2006 totaled $237.9 million, or 2.66% of total loans held for investment at December 31, 2006.

The following table sets forth information regarding non-performing loans as to which we have ceased accruing interest (dollars in thousands):

NON-ACCRUAL LOANS

	At December 31, 2007			
	Investment Loan Portfolio	Non-Accrual Loans	As a % of Loan Specified Portfolio	As a % of Non-Accrual Loans
Mortgage loans	$5,823,952	$134,551	2.31%	68.3%
Second mortgages	56,516	440	0.78%	0.2%
Commercial real estate	1,542,104	57,824	3.75%	29.3%
Construction	90,401	1,167	1.29%	0.6%
Warehouse lending	316,719	—	—%	—%
Consumer	281,746	3,167	1.12%	1.6%
Commercial non-real estate	22,959	—	—%	—%
Total loans	8,134,397	$197,149	2.42%	100.0%
Less allowance for loan losses	(104,000)			
Total loans held for investment portfolio (net of allowance)	$8,030,397			

Allowance for Loan Losses. The allowance for loan losses represents management's estimate of probable losses in our loans held for investment portfolio as of the date of the consolidated financial statements. The allowance provides for probable losses that have been identified with specific customer relationships and for probable losses believed to be inherent in the loan portfolio but that have not been specifically identified.

We perform a detailed credit quality review at least annually on large commercial loans as well as on selected other smaller balance commercial loans and may allocate a specific portion of the allowance to such loans based upon this review. Commercial and commercial real estate loans that are determined to be substandard and exceed $1.0 million are treated as impaired and are individually evaluated to determine the necessity of a specific reserve in accordance with the provisions of SFAS 114, *Accounting by Creditors for Impairment of a Loan.* This pronouncement requires a specific allowance to be established as a component of the allowance for loan losses when it is probable all amounts due will not be collected pursuant to the contractual terms of the loan and the recorded investment in the loan exceeds its fair value. Fair value is measured using either the present value of the expected future cash flows discounted at the loan's effective interest rate, the observable market price of the loan, or the fair value of the collateral if the loan is collateral dependent, reduced by estimated disposal costs. In estimating the fair value of collateral, we utilize outside fee-based appraisers to evaluate various factors, such as occupancy and rental rates in our real estate markets and the level of obsolescence that may exist on assets acquired from commercial business loans.

A portion of the allowance is also allocated to the remaining commercial loans by applying projected loss ratios, based on numerous factors identified below, to the loans within the different risk ratings.

Additionally, management has sub-divided the homogeneous portfolios, including consumer and residential mortgage loans, into categories that have exhibited a greater loss exposure (such as sub-prime loans and loans that are not salable on the secondary market because of collateral or documentation issues). The portion of the allowance allocated to other consumer and residential mortgage loans is determined by applying projected loss ratios to various segments of the loan portfolio. Projected loss ratios incorporate factors such as recent charge-off experience, current economic conditions and trends, trends with respect to past due and non-accrual amounts, and are supported by underlying analysis.

Management maintains an unallocated allowance to recognize the uncertainty and imprecision underlying the process of estimating expected loan losses. Determination of the probable losses inherent in the portfolio, which are not necessarily captured by the allocation methodology discussed above, involve the exercise of judgment.

As the process for determining the adequacy of the allowance requires subjective and complex judgment by management about the effect of matters that are inherently uncertain, subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for loan losses. In estimating the amount of credit losses inherent in our loan portfolio various assumptions are made. For example, when assessing the condition of the overall economic environment, assumptions are made regarding current economic trends and their impact on the loan portfolio. In the event the national economy were to sustain a prolonged downturn, the loss factors applied to our portfolios may need to be revised, which may significantly impact the measurement of the allowance for loan losses. For impaired loans that are collateral dependent, the estimated fair value of the collateral may deviate significantly from the proceeds received when the collateral is sold.

During the third quarter of 2007 and continuing in the fourth quarter of 2007, an increase in delinquency rates and an increase in seriously delinquent and non-performing loans, caused management to increase our overall allowance for loan losses. The overall delinquency rate (loans over 30 days delinquent using the OTS method) increased in 2007 to 4.03%, up from 1.34% as of December 31, 2006 and, for seriously delinquent loans (loans over 90 days delinquent using the OTS method), to 2.42% from 0.64%, respectively. At December 31, 2007, nonperforming loans totaled $197.1 million, an increase of $140.0 million over the amount at December 31, 2006. To better assess the extent of this credit exposure with respect to our commercial real estate portfolio, management conducted special reviews of commercial land and residential development loans with approximately $234.6 million of outstanding principal in the third quarter of 2007. As a result of these reviews, management downgraded a number of loans to substandard and special mention classification. Substantially all of the loans that were downgraded to substandard have been evaluated for impairment under the provisions of SFAS 114. During 2007, the provision for loan losses totaled $88.3 million, an increase of $62.9 million over the provisions for 2006.

The allowance for loan losses increased to $104.0 million at December 31, 2007 from $45.8 million at December 31, 2006. The allowance for loan losses as a percentage of non-performing loans decreased to 52.8% from 80.2% at December 31, 2006, which reflects the increase in non-accrual loans (i.e., loans over 90 days delinquent using the OTS method) to $197.1 million at December 31, 2007 compared to $57.1 million at December 31, 2006. The allowance for loan losses as a percentage of investment loans increased to 1.28% from 0.51% at December 31, 2006. As discussed above, the increase in the allowance for loan losses at December 31, 2007 reflects management's assessment of the effect of increased levels of impaired and adversely classified loans, increased delinquency rates in most loan categories, and increased levels of charge-offs.

The following tables set forth certain information regarding our allowance for loan losses as of December 31, and activity in the allowance for loan losses during the past five years:

ALLOWANCE FOR LOAN LOSSES

	At December 31, 2007			
	Investment Loan Portfolio	Percent of Portfolio	Reserve Amount	Percentage to Total Reserve
	(Dollars in thousands)			
Mortgage loans	$5,823,952	71.6%	$ 32,334	31.1%
Second mortgages	56,516	0.7	5,122	4.9
Commercial real estate	1,542,104	19.0	47,273	45.5
Construction	90,401	1.1	1,944	1.9
Warehouse lending	316,719	3.9	1,387	1.3
Consumer	281,746	3.4	13,064	12.6
Commercial non-real estate	22,959	0.3	680	0.6
Unallocated	—	—	2,196	2.1
Total	$8,134,397	100.0%	$104,000	100.0%

ALLOCATION OF THE ALLOWANCE FOR LOAN LOSSES

	At December 31,									
	2007		2006		2005		2004		2003	
	Reserve Amount	Loans To Total Loans	Reserve Amount	Loans To Total Loans	Reserve Amount	Loans To Total Loans	Reserve Amount	Loans To Total Loans	Reserve Amount	Loans To Total Loans
	(Dollars in thousands)									
Mortgage loans	$ 32,334	71.6%	$16,355	69.5%	$20,466	78.0%	$17,304	82.0%	$20,347	80.1%
Second mortgages	5,122	0.7%	6,627	8.0%	7,156	6.6%	3,318	1.9%	2,129	2.1%
Commercial real estate	47,273	19.0%	7,748	14.5%	5,315	9.4%	2,319	7.1%	7,532	8.0%
Construction	1,944	1.1%	762	0.7%	604	0.6%	3,538	0.6%	2,380	0.8%
Warehouse lending	1,387	3.9%	672	3.3%	334	1.4%	5,167	2.4%	273	5.1%
Consumer	13,064	3.4%	11,091	3.8%	3,396	3.9%	4,924	5.9%	3,710	3.8%
Commercial non- real estate	680	0.3%	362	0.2%	729	0.1%	1,748	0.1%	1,457	0.1%
Unallocated	2,196	—	2,162	—	1,140	—	—	—	—	—
Total	$104,000	100.0%	$45,779	100.0%	$39,140	100.0%	$38,318	100.0%	$37,828	100.0%

ACTIVITY IN THE ALLOWANCE FOR LOAN LOSSES

	For the Years Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Beginning balance	$ 45,779	$ 39,140	$ 38,318	$ 37,828	$ 39,389
Provision for loan losses	88,297	25,450	18,876	16,077	20,081
Charge-offs					
Mortgage loans	(17,468)	(9,833)	(11,853)	(14,629)	(20,455)
Consumer loans	(9,827)	(7,806)	(4,713)	(1,147)	(881)
Commercial loans	(4,765)	(1,414)	(3,055)	(680)	(1,048)
Construction loans	—	—	—	(2)	(313)
Other	(1,599)	(2,560)	(286)	(717)	(298)
Total charge offs	(33,659)	(21,613)	(19,907)	(17,175)	(22,995)
Recoveries					
Mortgage loans	687	665	1,508	1,081	641
Consumer loans	2,258	1,720	247	242	393
Commercial loans	174	40	98	265	114
Construction loans	—	—	—	—	—
Other	464	377	—	—	205
Total recoveries	3,583	2,802	1,853	1,588	1,353
Charge-offs, net of recoveries	(30,076)	(18,811)	(18,054)	(15,587)	(21,642)
Ending balance	$104,000	$ 45,779	$ 39,140	$ 38,318	$ 37,828
Net charge-off ratio	0.38%	0.20%	0.16%	0.16%	0.35%

Repossessed Assets. Real property that we acquire as a result of the foreclosure process is classified as "real estate owned" until it is sold. Management decides whether to rehabilitate the property or sell it "as is" and whether to list the property with a broker. Generally, we are able to dispose of a substantial portion of this type of real estate and other repossessed assets during each year, but we invariably acquire additional real estate and other assets through repossession in the ordinary course of business. At December 31, 2007, we had $109.3 million of repossessed assets compared to $81.0 million at December 31, 2006.

The following schedule provides the activity for repossessed assets during each of the past five years:

NET REPOSSESSED ASSET ACTIVITY

	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Beginning balance	$ 80,995	$ 47,724	$ 37,823	$ 36,778	$ 45,094
Additions	115,739	83,707	48,546	42,668	38,991
Disposals	(87,460)	(50,436)	(38,645)	(41,623)	(47,307)
Ending balance	$109,274	$ 80,995	$ 47,724	$ 37,823	$ 36,778

Repurchased Assets. We sell a majority of the mortgage loans we produce into the secondary market on a whole loan basis or by securitizing the loans into mortgage-backed securities. When we sell or securitize mortgage loans, we make customary representations and warranties to the purchasers about various characteristics of each loan, such as the manner of origination, the nature and extent of underwriting standards applied and the types of documentation being provided. When a loan that we have sold or securitized fails to perform according to its contractual terms, the purchaser will typically review the loan file to determine whether defects in the origination process occurred and if such defects constitute a violation of our representations and warranties. If there are no such defects, we have no liability to the purchaser for losses it may incur on such loan. If a defect is identified, we may be required to either repurchase the loan or indemnify the purchaser for losses it sustains on the loan. Loans that are repurchased and that are performing according to their terms are included within our loans held for investment portfolio. Repurchased assets are loans that we have reacquired because of representation and warranties issues related to loan sales or securitizations and that are non-performing at the time of repurchase. To the extent we later foreclose on the loan, the underlying property is transferred to repossessed assets for disposal. Upon obtaining title to such repurchased assets, the asset is transferred to repossessed assets for disposal. During 2007 and 2006, we repurchased $69.9 million and $68.4 million in unpaid principal balance of non-performing loans, respectively. The estimated fair value of the remaining repurchased assets totaled $9.6 million and $9.6 million at December 31, 2007 and 2006, respectively, and is included within other assets in our consolidated statements of financial condition.

The following table sets forth the underlying principal amount of non-performing loans we have repurchased or indemnified during the past five years, organized by the year of sale or securitization:

REPURCHASED ASSETS

Year	Total Loan Sales and Securitizations	Total Non-performing Repurchased Loans	% of Sales
	(Dollars in thousands)		
2003	$ 51,922,757	$ 34,924	0.07%
2004	28,937,576	57,794	0.20%
2005	24,703,575	46,721	0.19%
2006	16,968,994	17,668	0.10%
2007	24,710,651	1,945	0.01%
Totals	$147,243,553	$159,052	0.11%

Accrued Interest Receivable. Accrued interest receivable increased from $52.8 million at December 31, 2006 to $57.9 million at December 31, 2007 as our total earning assets increased. We typically collect interest in the month following the month in which it is earned.

FHLB Stock. Holdings of FHLB stock increased from $277.6 million at December 31, 2006, to $348.9 million at December 31, 2007. This increase was the result of the purchases of FHLB stock in 2007. As a member of the FHLB, we are required to hold shares of FHLB stock in an amount at least equal to 1.0% of the aggregate unpaid principal balance of our mortgage loans, home purchase contracts and similar obligations at the beginning of each year, or 1/20th of our FHLB advances, whichever is greater. Management believes that the volume of our holdings of FHLB stock do not constitute a controlling or significant interest in the FHLB. As such, management does not believe that the FHLB is an affiliate or can in any other way be deemed to be a related party.

Premises and Equipment. Premises and equipment, net of accumulated depreciation, totaled $237.6 million at December 31, 2007, an increase of $18.4 million, or 8.4%, from $219.2 million at December 31, 2006. During 2007, we added 13 additional banking centers and continued to invest in computer equipment. In addition, we acquired land for future bank expansion.

Mortgage Servicing Rights. Mortgage servicing rights totaled $414.0 million at December 31, 2007, an increase of $240.7 million, from $173.3 million at December 31, 2006. The increase reflects our capitalization of $346.3 million of MSRs, sales of $27.7 million of MSRs and amortization of $78.3 million of MSRs. The recorded amount of the MSR portfolio at December 31, 2007 and 2006 as a percentage of the unpaid principal balance of the loans we are servicing was 1.27% and 1.15%, respectively. When our home lending operation sells mortgage loans in the secondary market, it usually retains the right to continue to service the mortgage loans for a fee. The weighted average service fee on loans serviced for others is currently 0.36% of the loan principal balance outstanding. The amount of MSRs initially recorded is based on the fair value of the MSRs determined on the date when the underlying loan is sold. Our determination of fair value, and thus the amount we record (i.e., the capitalization amount) is based on estimated values paid by third party buyers in recent servicing rights sale transactions, internal valuations, and market pricing. Estimates of fair value reflect the following variables:

- Anticipated prepayment speeds (also known as the Constant Prepayment Rate)
- Product type (i.e., conventional, government, balloon)
- Fixed or adjustable rate of interest
- Interest rate
- Term (i.e. 15 or 30 years)
- Servicing costs per loan
- Discounted yield rate
- Estimate of ancillary income such as late fees, prepayment fees, etc.

The most important assumptions used in the MSR valuation model are anticipated annual loan prepayment speeds. During 2007, these speeds ranged between 16.3% and 28.7% on new production loans. The factors used for those assumptions are selected based on market interest rates and other market assumptions. Their reasonableness is confirmed through surveys conducted with independent third parties.

On an ongoing basis, the MSR portfolio is internally valued to assess any impairment in the asset. These impairment analyses consider the same variables that we address in determining the value of the portfolio at the financial statement date. In addition, a third party valuation of the MSR portfolio is obtained annually to confirm the reasonableness of the value generated by the internal valuation model.

At December 31, 2007 and 2006, the fair value of the MSR portfolio was $457.9 million and $197.6 million, respectively. At December 31, 2007, the fair value of each MSR was based upon the following weighted-average assumptions: (1) a discount rate of 9.2%; (2) an anticipated loan prepayment rate of 16.3% CPR; and (3) servicing costs per conventional loan of $42 and $45 for each government or adjustable-rate loan, respectively.

The following table sets forth activity in loans serviced for others during the past five years (dollars in thousands):

LOANS SERVICED FOR OTHERS ACTIVITY SCHEDULE

	For the Years Ended December 31,				
	2007	2006	2005	2004	2003
Balance, beginning of year	$15,032,504	$ 29,648,088	$21,354,724	$ 30,395,079	$ 21,586,797
Loan servicing capitalized	24,255,114	16,370,925	21,595,729	27,584,787	49,461,431
Loan amortization/prepayments	(3,248,986)	(3,376,219)	(4,220,504)	(6,985,894)	(9,982,414)
Loan servicing sales	(3,551,295)	(27,610,290)	(9,081,861)	(29,639,248)	(30,670,735)
Balance, end of year	$32,487,337	$ 15,032,504	$29,648,088	$ 21,354,724	$ 30,395,079

Other Assets. Other assets increased $12.1 million, or 9.5%, to $138.6 million at December 31, 2007, from $126.5 million at December 31, 2006. The majority of this increase was attributable to an increase of $4.4 million in the fair value of derivatives and an increase in escrow advances of $6.1 million.

Liabilities

Deposits. Deposit accounts increased $0.6 billion, or 7.9%, to $8.2 billion at December 31, 2007, from $7.6 billion at December 31, 2006. We increased the number of banking centers from 151 at December 31, 2006 to 164 at December 31, 2007.

Our deposits can be subdivided into four areas: the retail division, the municipal division, the national accounts division and Company controlled deposits. Retail deposit accounts increased $0.2 billion, or 3.5% to $5.1 billion at December 31, 2007, from $4.9 billion at December 31, 2006. Saving and checking accounts totaled 13.28% of total retail deposits. In addition, at December 31, 2007, retail certificates of deposit totaled $3.9 billion, with an average balance of $25,911 and a weighted average cost of 5.0% while money market deposits totaled $531.6 million, with an average cost of 3.9%. Overall, the retail division had an average cost of deposits of 4.5% at December 31, 2007 versus 4.4% at December 31, 2006.

We call on local municipal agencies as another source for deposit funding. Municipal deposits increased $0.1 billion or 7.1% to $1.5 billion at December 31, 2007, from $1.4 billion at December 31, 2006. These balances fluctuate during the year as the municipalities collect semi-annual assessments and make necessary disbursements over the following six-months. These deposits had a weighted average cost of 5.0% at December 31, 2007. These deposit accounts include $1.5 billion of certificates of deposit with maturities typically less than one year and $72.0 million in checking and savings accounts.

In past years, our national accounts division garnered wholesale deposits through nationwide advertising of deposit rates and the use of investment banking firms. For the years ended December 31, 2006 and 2005 and through June 30 2007, we did not solicit any funds through the division as we were able to access more attractive funding sources through FHLB advances, security repurchase agreements and other forms of deposits that provide the potential for a long term customer relationship. Beginning in July 2007, wholesale deposits became attractive from a cost of funds standpoint, so we began to solicit funds through our national accounts division. These deposit accounts increased $79.0 million, or 7.4%, to $1.1 billion at December 31, 2007, from the December 31, 2006 deposit amount. These deposits had a weighted average cost of 4.6% at December 31, 2007.

Company controlled deposits are accounts that represent the portion of the investor custodial accounts controlled by Flagstar that have been placed on deposit with the Bank. These deposits do not bear interest. Company controlled deposits increased $229.2 million to $473.4 million at December 31, 2007 from $244.2 million at December 31, 2006. This increase is the result of our increase in mortgage loans being serviced for others during 2007.

The deposit accounts are as follows at December 31, (dollars in thousands):

	At December 31,	
	2007	2006
Demand accounts	$ 436,239	$ 380,162
Savings accounts	237,762	144,460
MMDA	531,587	608,282
Certificates of deposit(1)	3,870,828	3,763,781
Total retail deposits	5,076,416	4,896,685
Municipal deposits	1,545,395	1,419,964
National accounts	1,141,549	1,062,646
Company controlled deposits	473,384	244,193
Total deposits	$8,236,744	$7,623,488

(1) The aggregate amount of certificates of deposit with a minimum denomination of $100,000 was approximately $2.8 billion and $2.6 billion at December 31, 2007 and December 31, 2006, respectively.

Interest Rate Swaps. In October 2003, we entered into a series of interest rate swaps to offset our exposure to rising rates on a portion of our certificates of deposit portfolio. The notional amount of these swaps totaled $500 million. Contractually, we receive a floating rate tied to LIBOR and pay a fixed rate. The swaps are categorized in two groups: the first receiving one-month LIBOR and the second receiving three-month LIBOR. These swaps have maturities ranging from three to five years. These interest rate swaps effectively act as a cash flow hedge against a rise in the cost of our deposits. On December 30, 2004, we extinguished $250 million of the swaps for an after-tax gain of $2.6 million. This gain was deferred and was reclassified into earnings from accumulated other comprehensive income (loss) over three years, which was the original duration of the extinguished swaps. At December 31, 2007, we had $105.0 million (notional amount) of these interest rate swap agreements outstanding.

On December 19, 2002, we, through our subsidiary Flagstar Statutory Trust II, completed a private placement sale of trust-preferred securities. As part of the transaction, we entered into an interest rate swap agreement with the placement agent in which we pay a fixed rate of 6.88% on a notional amount of $25.0 million and receive a floating rate equal to that being paid on the Flagstar Statutory Trust II securities. This swap matured in December 2007.

On September 22, 2005, we, through our subsidiary Flagstar Statutory Trust VIII, completed a private placement sale of trust-preferred securities. As part of the transaction, we entered into an interest rate swap with the placement agent in which we are required to pay a fixed rate of 4.33% on a notional amount of $25.0 million and will receive a floating rate equal to that being paid on the Flagstar Statutory Trust VIII securities. The swap matures on October 7, 2010. The securities are callable after October 7, 2010.

FHLB Advances. FHLB advances increased $0.9 billion, or 16.7%, to $6.3 billion at December 31, 2007, from $5.4 billion at December 31, 2006. We rely upon advances from the FHLB as a source of funding for the origination or purchase of loans for sale in the secondary market and for providing duration-specific short-term and medium-term financing. The outstanding balance of FHLB advances fluctuates from time to time depending upon our current inventory of mortgage loans available for sale and the availability of lower cost funding from our deposit base, the escrow accounts we hold, or alternative funding sources such as repurchase agreements. See Note 13 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplemental Data, herein for additional information on FHLB advances.

The $1.9 billion portfolio of putable FHLB advances we hold, which matures in 2012, may be called by the FHLB based on FHLB volatility models. If these advances are called, we will be forced to find an alternative source of funding, which could be at a higher cost and, therefore, negatively impact net earnings.

Security Repurchase Agreements. Security repurchase agreements declined $882.8 million to $108.0 million at December 31, 2007, from $990.8 million at December 31, 2006. Securities sold under agreements to repurchase are generally accounted for as collateralized financing transactions and are recorded at the amounts at which the securities were sold plus accrued interest. Securities, generally mortgage backed securities, are pledged as collateral under these financing arrangements. The fair value of collateral provided to a party is continually monitored, and additional collateral is obtained or requested to be returned, as appropriate. See Note 14 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplemental Data, herein, for additional information on security repurchase agreements.

Long-Term Debt. As part of our overall capital strategy, we may raise capital through the issuance of trust-preferred securities by our special purpose financing entities formed for the offerings. The trust preferred securities outstanding mature 30 years from issuance, are callable after five years, pay interest quarterly, and the interest expense is deductible for federal income tax purposes. The majority of the net proceeds from these offerings was contributed to the Bank as additional paid in capital and subject to regulatory limitations, is includable as regulatory capital. Under these arrangements, we have the right to defer dividend payments to the trust preferred security holders for up to five years.

On December 19, 2002, we, through our subsidiary Flagstar Statutory Trust II, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $25.0 million. The securities pay interest at a floating rate of three-month LIBOR plus 3.25%, adjustable quarterly, after an initial rate of

4.66%. As part of the transaction, we entered into an interest rate swap agreement with the placement agent in which we pay a fixed rate of 6.88% on a notional amount of $25.0 million and receive a floating rate equal to that being paid on the Flagstar Statutory Trust II securities. The interest rate swap matured in December 2007.

On February 19, 2003, we, through our subsidiary Flagstar Statutory Trust III, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $25.0 million. The securities have an effective cost for the first five years of 6.55% and a floating rate thereafter equal to the three-month LIBOR rate plus 3.25% adjustable quarterly.

On March 19, 2003, we, through our subsidiary Flagstar Statutory Trust IV, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $25.0 million. The securities have an effective cost for the first five years of 6.75% and a floating rate thereafter equal to the three-month LIBOR rate plus 3.25% adjustable quarterly.

On December 29, 2004, we, through our subsidiary Flagstar Statutory Trust V, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $25.0 million. The securities have a floating rate that reprices quarterly at three-month LIBOR plus 2.00%.

On March 30, 2005, we, through our subsidiary Flagstar Statutory Trust VI, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $25.0 million. The securities have a floating rate that reprices quarterly at three-month LIBOR plus 2.00%.

On March 31, 2005, we, through our subsidiary Flagstar Statutory Trust VII, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $50.0 million. The securities have an effective cost for the first five years of 6.47% and a floating rate thereafter equal to the three-month LIBOR rate plus 2.00% adjustable quarterly.

On September 22, 2005, we, through our subsidiary Flagstar Statutory Trust VIII, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $25.0 million. The securities have a floating rate that reprices quarterly at three-month LIBOR plus 1.50%.

On June 28, 2007, we, through our subsidiary Flagstar Statutory Trust IX, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $25.0 million. The securities have a floating rate that reprices quarterly at three-month LIBOR plus 1.45%.

On August 31, 2007, we, through our subsidiary Flagstar Statutory Trust X, completed a private placement sale of trust-preferred securities, providing gross proceeds totaling $15.0 million. The securities have a floating rate that reprices quarterly at three-month LIBOR plus 2.50%.

Accrued Interest Payable. Accrued interest payable increased $0.8 million, or 1.7%, to $47.1 million at December 31, 2007 from $46.3 million at December 31, 2006. These amounts represent interest payments that are payable to depositors and other entities from which we borrowed funds. These balances fluctuate with the size of our interest-bearing liability portfolio and the average cost of our interest-bearing liabilities. The interest-bearing liability portfolio increased 8.7% during the period and we had a 0.4% increase in the average cost of liabilities to 4.72%.

Undisbursed Payments. Undisbursed payments on loans serviced for others increased $35.0 million, or 376.3%, to $44.3 million at December 31, 2007, from $9.3 million at December 31, 2006. These amounts represent payments received from borrowers for interest, principal and related loan charges, which have not been remitted to loan investors. These balances fluctuate with the size of the servicing portfolio and the transferring of servicing to the purchaser in connection with servicing sales. Loans serviced for others at December 31, 2007, including subservicing of $0.5 billion, equaled $33.0 billion versus $15.2 billion at December 31, 2006.

Federal Income Taxes Payable (Receivable). Income taxes payable decreased, to a receivable of $28,000 at December 31, 2007, from $29.7 million at December 31, 2006. The Federal income taxes receivable is recorded in other assets on our consolidated statement of financial condition at December 31, 2007. See

Note 16 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplementary Data, herein.

Secondary Market Reserve. We sell most of the residential mortgage loans that we originate into the secondary mortgage market. When we sell mortgage loans we make customary representations and warranties to the purchasers about various characteristics of each loan, such as the manner of origination, the nature and extent of underwriting standards applied and the types of documentation being provided. Typically these representations and warranties are in place for the life of the loan. If a defect in the origination process is identified, we may be required to either repurchase the loan or indemnify the purchaser for losses it sustains on the loan. If there are no such defects, we have no liability to the purchaser for losses it may incur on such loan. We maintain a secondary market reserve to account for the expected losses related to loans we might be required to repurchase (or the indemnity payments we may have to make to purchasers). The secondary market reserve takes into account both our estimate of expected losses on loans sold during the current accounting period, as well as adjustments to our previous estimates of expected losses on loans sold. In each case these estimates are based on our most recent data regarding loan repurchases, actual credit losses on repurchased loans and recovery history, among other factors. Increases to the secondary market reserve for current loan sales reduce our net gain on loan sales. Adjustments to our previous estimates are recorded as an increase or decrease in our other fees and charges. The amount of the secondary market reserve equaled $27.6 million and $24.2 million at December 31, 2007 and 2006, respectively. See Note 17 of the Notes to the Consolidated Financial Statements, in Item 8. Financial Statements and Supplemental Data, herein.

Contractual Obligations and Commitments

We have various financial obligations, including contractual obligations and commercial commitments, which require future cash payments. Refer to Item 8. Financial Statements and Supplemental Data Notes 2, 10, 12, 13, 14 and 15. The following table presents the aggregate annual maturities of contractual obligations (based on final maturity dates) at December 31, 2007 (dollars in thousands):

	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years	Total
Deposits without stated maturities	$1,277,928	$ —	$ —	$ —	$ 1,277,928
Certificates of deposits	5,368,021	952,952	155,683	8,776	6,485,432
FHLB advances	1,851,000	1,300,000	2,650,000	500,000	6,301,000
Trust preferred securities	—	—	—	247,435	247,435
Operating leases	6,335	8,255	3,084	1,635	19,309
Security repurchase agreements	108,000	—	—	—	108,000
Other debt	25	50	50	1,125	1,250
Total	$8,611,309	$2,261,257	$2,808,817	$758,971	$14,440,354

Included in the FHLB advances above are putable advances amounting to $1.6 billion that may be called by the FHLB during 2008 and thereafter and $0.3 billion of putable advances that may be called in 2009 and thereafter.

Liquidity and Capital Resources

Our principal uses of funds include loan originations, operating expenses, the payment of dividends and stock repurchases. At December 31, 2007, we had outstanding rate-lock commitments to lend $3.2 billion in mortgage loans, along with outstanding commitments to make other types of loans totaling $110.9 million. These commitments may expire without being drawn upon and, therefore, do not necessarily represent future cash requirements. Total commercial and consumer unused collateralized lines of credit totaled $1.7 billion at December 31, 2007.

We suffered a loss in excess of $39 million during 2007 and as a result, saw our shareholders' equity and regulatory capital decline in the second half of the year. While we currently have regulatory capital ratios in excess of the "well capitalized" requirement, there can be no assurance that we will not suffer additional losses or that additional capital will not otherwise be required for regulatory or other reasons. In those circumstances, we may be required to obtain additional capital to maintain our regulatory capital ratios at the "well capitalized" level. Such capital raising could be at terms that are dilutive to existing shareholders and there can be no assurance that any capital raising we undertake would be successful given the current level of disruption in financial markets.

We paid a total cash dividend of $21.4 million on our common stock during 2007. Any payment of dividends in the future is subject to the determination of our Board of Directors. On February 19, 2008, our Board of Directors suspended future dividends payable on our common stock. Under the capital distribution regulations, a savings association that is a subsidiary of a savings and loan holding company must either notify or seek approval from the OTS of an association capital distribution at least 30 days prior to the declaration of a dividend or the approval by the Board of Directors of the proposed capital distribution. The 30-day period allows the OTS to determine whether the distribution would not be advisable. We currently must seek approval from the OTS prior to making a capital distribution from the Bank.

On January 31, 2007, the Company announced that the Board of Directors had adopted a Stock Repurchase Program under which the Company was authorized to repurchase up to $40.0 million worth of outstanding common stock. On February 27, 2007, the Company announced that the Board of Directors had increased the authorized repurchase amount to $50.0 million. On April 26, 2007, the Board increased the authorized repurchase amount to $75.0 million. This program expired on January 31, 2008. At December 31, 2007, $41.7 million had been used to repurchase 3.4 million shares under the program.

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by regulators about components, risk weightings, and other factors.

Our primary sources of funds are customer deposits, loan repayments and sales, advances from the FHLB, repurchase agreements, cash generated from operations, and customer escrow accounts. Additionally, we have issued trust preferred securities in eight separate offerings to the capital markets. We believe that these sources of capital will continue to be adequate to meet our liquidity needs for the foreseeable future. The following sets forth certain additional information regarding our sources of liquidity.

Deposits. The following table sets forth information relating to our total deposit flows for each of the years indicated:

	For the Years Ended December 31,				
	2007	2006	2005	2004	2003
	(Dollars in thousands)				
Beginning deposits	$7,623,488	$ 8,521,756	$7,433,776	$5,729,650	$4,435,182
Interest credited	357,430	331,516	253,292	167,765	138,625
Net deposit increase (decrease)	255,826	(1,229,784)	834,688	1,536,361	1,155,843
Total deposits, end of the year	$8,236,744	$ 7,623,488	$8,521,756	$7,433,776	$5,729,650

Borrowings. The FHLB provides credit for savings institutions and other member financial institutions. We are currently authorized through a board resolution to apply for advances from the FHLB using our mortgage loans as collateral. We currently have an authorized line of credit equal to $7.5 billion, secured by eligible residential mortgage loans. At December 31, 2007, we had available collateral sufficient to access $7.0 billion of the line and had $6.3 billion of FHLB advances outstanding at December 31, 2007.

During May 2007, we completed arrangements with the Federal Reserve Bank of Chicago to borrow as needed from its discount window. The discount window is a borrowing facility that is intended to be used only for short-term liquidity needs arising from special or unusual circumstances. The amount we are allowed to borrow is based on the lendable value of the collateral that we provide. To collateralize the line, we pledge commercial loans that are eligible based on Federal Reserve Bank of Chicago guidelines. At December 31, 2007, we had pledged commercial loans amounting to $1.1 billion with a lendable value of $0.8 billion. At December 31, 2007, we had no borrowings outstanding against this line of credit.

Security Repurchase Agreements. Securities sold under agreements to repurchase are generally accounted for as collateralized financing transactions and are recorded at the amounts at which the securities were sold plus accrued interest. Securities, generally mortgage backed securities, are pledged as collateral under these financing arrangements. The fair value of collateral provided to a party is continually monitored and additional collateral is obtained or requested to be returned, as appropriate. At December 31, 2007, security repurchase agreements amounted to $108.0 million. Also at December 31, 2007, security repurchase agreements were secured by $115.0 million of mortgage-backed securities held to maturity.

Loan Sales. Our home lending operation sells a significant portion of the mortgage loans that it originates. Sales of loans totaled $23.3 billion, or 90.7% of originations in 2007, compared to $16.0 billion, or 84.2% of originations, in 2006. The increase in sales during 2007 was attributable to the increase in originations and the decreased amount of loans retained by us for our own portfolio. As of December 31, 2007, we had outstanding commitments to sell $3.8 billion of mortgage loans. Generally, these commitments are funded within 120 days.

Loan Principal Payments. In our capacity as an investor in loans, we derive funds from the repayment of principal on the loans we hold in portfolio. Payments totaled $2.8 billion and $3.9 billion during 2007 and 2006, respectively.

LOAN REPAYMENT SCHEDULE

	At December 31, 2007							
	Within 1 Year	1 Year to 2 Years	2 Years to 3 Years	3 Years to 5 Years	5 Years to 10 Years	10 Years to 15 Years	Over 15 Years	Totals
	(Dollars in thousands)							
Mortgage loans	$ 82,565	$ 75,140	$ 74,149	$146,340	$356,194	$332,691	$4,709,216	$5,776,295
Second mortgage	1,897	1,833	1,771	3,424	7,984	6,642	32,863	56,414
Commercial real estate	164,081	146,638	131,033	236,741	464,667	215,028	185,217	1,543,405
Construction	90,306	—	—	—	—	—	—	90,306
Warehouse lending	316,719	—	—	—	—	—	—	316,719
Consumer	18,501	16,797	15,717	29,416	63,410	43,722	92,394	279,957
Commercial non-real estate	5,114	3,975	3,089	4,803	5,978	—	—	22,959
Total	$679,183	$244,383	$225,759	$420,724	$898,233	$598,083	$5,019,690	$8,086,055

Escrow Funds. As a servicer of mortgage loans, we hold funds in escrow for investors, various insurance entities, or for the government taxing authorities. At December 31, 2007, we held $37.8 million in these escrows.

Impact of Off-Balance Sheet Arrangements

Financial Interpretation ("FIN") FIN 46R requires us to separately report, rather than include in our consolidated financial statements, the separate financial statements of our wholly-owned subsidiaries Flagstar Trust, Flagstar Statutory Trust II, Flagstar Statutory Trust III, Flagstar Statutory Trust IV, Flagstar Statutory Trust V, Flagstar Statutory Trust VI, Flagstar Statutory Trust VII, Flagstar Statutory Trust VIII, Flagstar

Statutory Trust IX and Flagstar Statutory Trust X. We did this by reporting our investment in these entities under "other assets."

Asset Securitization. The Bank, in its efforts to diversify its funding sources, occasionally transfers loans to a qualifying special purpose entity ("QSPE") in a process known as a securitization in exchange for asset-backed securities. A QSPE is generally a trust that is severely limited in permitted activities, assets it may hold, sell, exchange or distribute. When a company transfers assets to a QSPE, the transfer is generally treated as a sale and the transferred assets are no longer recognized on the transferor's balance sheet. The QSPE in turn will offer the sold loans to investors in the form of a security. The proceeds the QSPE receives from investors are used to pay the company for the loans sold. The company will usually recognize a gain or loss on the transfer. Statements of Financial Accounting Standards (SFAS) 140, *Accounting for the Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, provides specific criteria to meet the definition of a QSPE. QSPE's are required to be legally isolated from the transferor and bankruptcy remote, insulating investors from the impact of creditors of other entities, including the transferor, and are not consolidated within the financial statements.

When a company sells or securitizes loans it generally retains the servicing rights of those loans and may retain senior, subordinated, residual interests all of which are considered retained interest on the loans sold. Retained interests in securitizations were $47.0 million and $42.5 million at December 31, 2007 and 2006, respectively. Additional information concerning securitization transactions is included in Note 7 in the Notes to our Consolidated Financial Statements, in Item 8 Financial Statements and Supplemental Data, herein.

Impact of Inflation and Changing Prices

The Consolidated Financial Statements and Notes thereto presented herein have been prepared in accordance with U.S. GAAP, which requires the measurement of financial position and operating results in terms of historical dollars without considering the changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of our operations. Unlike most industrial companies, nearly all of our assets and liabilities are monetary in nature. As a result, interest rates have a greater impact on our performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

Accounting and Reporting Developments

See Note 2 of the Notes to the Consolidated Financial Statements, Item 8 Financial Statements and Supplementary Data, herein for details of recently issued accounting pronouncements and their expected impact on our consolidated financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the risk of loss arising from adverse changes in the fair value of financial instruments due to changes in interest rates, currency exchange rates, or equity prices. We do not have any material foreign currency exchange risk or equity price risk. Interest rate risk is our primary market risk and results from timing differences in the repricing of assets and liabilities, changes in the relationships between rate indices, and the potential exercise of explicit or embedded options.

Interest rate risk is managed by the Executive Investment Committee ("EIC"), which is composed of several of our executive officers and other members of management, in accordance with policies approved by our Board of Directors. The EIC formulates strategies based on appropriate levels of interest rate risk. In determining the appropriate level of interest rate risk, the EIC considers the impact projected interest rate scenarios have on earnings and capital, liquidity, business strategies, and other factors. The EIC meets monthly or as deemed necessary to review, among other things, the sensitivity of assets and liabilities to interest rate changes, the book and fair values of assets and liabilities, unrealized gains and losses, purchase and sale activity, loans available for sale and commitments to originate loans, and the maturities of investments, borrowings and time deposits. Any decision or policy change that requires implementation is directed to the

Asset and Liability Committee ("ALCO"). The ALCO implements any directive from the EIC and meets weekly to monitor liquidity, cash flow flexibility and deposit activity.

Financial instruments used to manage interest rate risk include financial derivative products such as interest rate swaps and forward sales commitments. Further discussion of the use of and the accounting for derivative instruments is included in Notes 2 and 24 to the consolidated financial statements in Item 8 of this report. All of our derivatives are accounted for at fair market value. Although we have and will continue to economically hedge a portion of our mortgage loans available for sale, on October 1, 2005, for financial reporting purposes, we dedesignated all fair value hedges that solely related to our mortgage lending operation. This means that changes in the fair value of our forward sales commitments will not necessarily be offset by corresponding changes in the fair value of our mortgage loans available for sale because the mortgage loans available for sale are recorded at the lower of cost or market. In the future, additional volatility may be introduced into our consolidated financial statements.

To effectively measure and manage interest rate risk, we use sensitivity analysis to determine the impact on net market value of various interest rate scenarios, balance sheet trends, and strategies. From these simulations, interest rate risk is quantified and appropriate strategies are developed and implemented. Additionally, duration and net interest income sensitivity measures are utilized when they provide added value to the overall interest rate risk management process. The overall interest rate risk position and strategies are reviewed by our executive management and our Board of Directors on an ongoing basis. We have traditionally managed our business to reduce our overall exposure to changes in interest rates. However, management has the latitude to increase our interest rate sensitivity position within certain limits if, in management's judgment, the increase will enhance profitability.

In the past, the savings and loan industry measured interest rate risk using gap analysis. Gap analysis is one indicator of interest rate risk; however it only provides a glimpse into expected asset and liability repricing in segmented time frames. Today the thrift industry utilizes the concept of Net Portfolio Value ("NPV"). NPV analysis provides a fair value of the balance sheet in alternative interest rate scenarios. The NPV does not take into account management intervention and assumes the new rate environment is constant and the change is instantaneous.

The following table is a summary of the changes in our NPV that are projected to result from hypothetical changes in market interest rates. NPV is the market value of assets, less the market value of liabilities, adjusted for the market value of off-balance sheet instruments. The interest rate scenarios presented in the table include interest rates at December 31, 2007 and 2006 and as adjusted by instantaneous parallel rate changes upward to 300 basis points and downward to 200 basis points. The 2007 and 2006 scenarios are not comparable due to differences in the interest rate environments, including the absolute level of rates and the shape of the yield curve. Each rate scenario reflects unique prepayment, repricing, and reinvestment assumptions. Management derives these assumptions by considering published market prepayment expectations, the repricing characteristics of individual instruments or groups of similar instruments, our historical experience, and our asset and liability management strategy. Further, this analysis assumes that certain instruments would not be affected by the changes in interest rates or would be partially affected due to the characteristics of the instruments.

This analysis is based on our interest rate exposure at December 31, 2007 and 2006, and does not contemplate any actions that we might undertake in response to changes in market interest rates, which could impact NPV. Further, as this framework evaluates risks to the current statement of financial condition only, changes to the volumes and pricing of new business opportunities that can be expected in the different interest rate outcomes are not incorporated in this analytical framework. For instance, analysis of our history suggests that declining interest rate levels are associated with higher loan production volumes at higher levels of profitability. While this "natural business hedge" historically offset most, if not all, of the identified risks associated with declining interest rate scenarios, these factors fall outside of the net portfolio value framework. Further, there can be no assurance that this natural business hedge would positively affect the net portfolio value in the same manner and to the same extent as in the past because the current rate scenario reflects a decline in the Federal Funds rate but an increase (rather than concurrent decrease) in rates for residential home mortgage loans.

There are limitations inherent in any methodology used to estimate the exposure to changes in market interest rates. It is not possible to fully model the market risk in instruments with leverage, option, or prepayment risks. Also, we are affected by basis risk, which is the difference in repricing characteristics of similar term rate indices. As such, this analysis is not intended to be a precise forecast of the effect a change in market interest rates would have on us.

While each analysis involves a static model approach to a dynamic operation, the NPV model is the preferred method. If NPV rises in an up or down interest rate scenario, that would indicate an up direction for the margin in that hypothetical rate scenario. A perfectly matched balance sheet would possess no change in the NPV, no matter what the rate scenario. The following table presents the NPV in the stated interest rate scenarios (dollars in millions):

At December 31,									
2007					2006				
Scenario	NPV	NPV%	$ Change	% Change	Scenario	NPV	NPV%	$ Change	% Change
300	$1,013	6.69%	$(203)	(16.7)%	300	$ 908	6.19%	$(428)	(32.0)%
200	1,160	7.48	(56)	(4.6)	200	1,099	7.32	(237)	(17.7)
100	1,254	7.92	(38)	3.2	100	1,257	8.19	(79)	(5.9)
Current	1,216	7.56	—	—	Current	1,336	8.56	—	—
−100	964	5.98	(252)	(20.7)	−100	1,281	8.14	(55)	(4.1)
−200	730	4.51	(486)	(40.0)	−200	1,206	7.62	(130)	(9.8)

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Index to Consolidated Financial Statements

March 12, 2008

Management's Report

Flagstar Bancorp's management is responsible for the integrity and objectivity of the information contained in this document. Management is responsible for the consistency of reporting this information and for ensuring that accounting principles generally accepted in the United States of America are used.

In discharging this responsibility, management maintains a comprehensive system of internal controls and supports an extensive program of internal audits, has made organizational arrangements providing appropriate divisions of responsibility and has established communication programs aimed at assuring that its policies, procedures and principles of business conduct are understood and practiced by its employees.

The consolidated statements of financial condition as of December 31, 2007 and 2006 and the related statements of operation, stockholders' equity and comprehensive income (loss) and cash flows for each of the three years in the period ended December 31, 2007, 2006 and 2005 included in this document have been audited by Virchow, Krause & Company, LLP, an independent registered public accounting firm. All audits were conducted using standards of the Public Company Accounting Oversight Board (United States) and the independent registered public accounting firms' reports and consents are included herein.

The Board of Directors' responsibility for these consolidated financial statements is pursued mainly through its Audit Committee. The Audit Committee is composed entirely of directors who are not officers or employees of Flagstar Bancorp, Inc., and meets periodically with the internal auditors and independent registered public accounting firm, both with and without management present, to assure that their respective responsibilities are being fulfilled. The internal auditors and independent registered public accounting firm have full access to the Audit Committee to discuss auditing and financial reporting matters.

/s/ Mark T. Hammond
Mark T. Hammond
President and Chief Executive Officer

/s/ Paul D. Borja
Paul D. Borja
Executive Vice-President and Chief Financial Officer

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders
Flagstar Bancorp, Inc.

We have audited the accompanying consolidated statements of financial condition of Flagstar Bancorp, Inc. and subsidiaries (the "Company") as of December 31, 2007 and 2006, and the related consolidated statements of operations, shareholders' equity and comprehensive income (loss) and cash flows for each of the three years in the period ended December 31, 2007. We also have audited the Company's internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Flagstar Bancorp Inc. and subsidiaries as of December 31, 2007 and 2006, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, Flagstar Bancorp, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

/s/ Virchow, Krause & Company, LLP
Southfield, Michigan
March 12, 2008

Flagstar Bancorp, Inc.
Consolidated Statements of Financial Condition
(In thousands, except share data)

	At December 31, 2007	At December 31, 2006
Assets		
Cash and cash items	$ 129,992	$ 136,675
Interest-bearing deposits	210,177	140,561
Cash and cash equivalents	340,169	277,236
Securities classified as trading	13,703	—
Securities classified as available for sale	1,308,608	617,450
Mortgage-backed securities held to maturity (fair value $1.3 billion and $1.6 billion at December 31, 2007 and December 31, 2006, respectively)	1,255,431	1,565,420
Other investments	26,813	24,035
Loans available for sale	3,511,310	3,188,795
Loans held for investment	8,134,397	8,939,685
Less: allowance for loan losses	(104,000)	(45,779)
Loans held for investment, net	8,030,397	8,893,906
Total interest-earning assets	14,356,439	14,430,167
Accrued interest receivable	57,888	52,758
Repossessed assets, net	109,274	80,995
Federal Home Loan Bank stock	348,944	277,570
Premises and equipment, net	237,652	219,243
Mortgage servicing rights, net	413,986	173,288
Other assets	138,561	126,509
Total assets	$15,792,736	$15,497,205
Liabilities and Stockholders' Equity		
Liabilities		
Deposits	$ 8,236,744	$ 7,623,488
Federal Home Loan Bank advances	6,301,000	5,407,000
Security repurchase agreements	108,000	990,806
Long term debt	248,685	207,472
Total interest-bearing liabilities	14,894,429	14,228,766
Accrued interest payable	47,070	46,302
Secondary market reserve	27,600	24,200
Payable for securities purchased	—	249,694
Other liabilities	130,659	136,009
Total liabilities	15,099,758	14,684,971
Commitments and Contingencies — Note 19		
Stockholders' Equity		
Common stock $0.01 par value, 150,000,000 shares authorized; 63,656,979 and 63,604,590 shares issued; 60,270,624 and 63,604,590 outstanding at December 31, 2007 and December 31, 2006, respectively	637	636
Additional paid in capital	64,350	63,223
Accumulated other comprehensive (loss) income	(11,495)	5,182
Retained earnings	681,165	743,193
Treasury stock, at cost, 3,386,355 shares at December 31, 2007, and none at December 31, 2006	(41,679)	—
Total stockholders' equity	692,978	812,234
Total liabilities and stockholders' equity	$15,792,736	$15,497,205

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

Flagstar Bancorp, Inc.
Consolidated Statements of Operations
(In thousands, except per share data)

	For the Years Ended December 31,		
	2007	2006	2005
Interest Income			
Loans	$769,485	$711,037	$688,791
Mortgage-backed securities	59,960	77,607	19,019
Securities available for sale	56,578	4,183	—
Interest-bearing deposits	12,949	3,041	—
Other	6,537	4,998	853
Total interest income	905,509	800,866	708,663
Interest Expense			
Deposits	357,430	331,516	253,292
FHLB advances	271,443	187,756	182,377
Security repurchase agreements	51,458	52,389	7,953
Other	15,300	14,258	18,771
Total interest expense	695,631	585,919	462,393
Net interest income	209,878	214,947	246,270
Provision for loan losses	88,297	25,450	18,876
Net interest income after provision for loan losses	121,581	189,497	227,394
Non-Interest Income			
Loan fees and charges	1,497	7,440	12,603
Deposit fees and charges	22,999	20,893	16,918
Loan administration	12,715	13,032	8,761
Net gain on loan sales	59,030	42,381	63,580
Net gain on sales of mortgage servicing rights	5,898	92,621	18,157
Net loss on securities available for sale	(16,679)	(6,163)	—
Loss on trading securities	(6,785)	—	—
Other fees and charges	38,440	31,957	39,429
Total non-interest income	117,115	202,161	159,448
Non-Interest Expense			
Compensation and benefits	168,559	140,438	126,139
Occupancy and equipment	69,122	70,225	69,007
Communication	5,400	4,320	4,840
Other taxes	(1,756)	320	7,844
General and administrative	56,185	60,334	55,057
Total non-interest expense	297,510	275,637	262,887
(Loss) earnings before federal tax provision	(58,814)	116,021	123,955
(Benefit) provision for federal income taxes	(19,589)	40,819	44,090
Net (Loss) Earnings	$ (39,225)	$ 75,202	$ 79,865
(Loss) earnings per share			
Basic	$ (0.64)	$ 1.18	$ 1.29
Diluted	$ (0.64)	$ 1.17	$ 1.25

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

Flagstar Bancorp, Inc.
Consolidated Statements of Stockholders' Equity and Comprehensive Income (Loss)
(In thousands, except per share data)

	Common Stock	Additional Paid in Capital	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Retained Earnings	Total Stockholders' Equity
Balance at January 1, 2005	$614	$40,754	$ 5,343	$ —	$682,243	$728,954
Net earnings	—	—	—	—	79,865	79,865
Reclassification of gain on swap extinguishment	—	—	(1,335)	—	—	(1,335)
Change in net unrealized gain on swaps used in cash flow hedges	—	—	3,328	—	—	3,328
Change in net unrealized gain on securities available for sale	—	—	498	—	—	498
Total comprehensive income	—	—	—	—	—	82,356
Stock options exercised	18	7,426	—	—	—	7,444
Stock-based compensation	—	745	—	—	—	745
Tax benefit from stock-based compensation	—	8,379	—	—	—	8,379
Dividends paid ($0.90 per share)		—	—	—	(55,995)	(55,995)
Balance at December 31, 2005	632	57,304	7,834	—	706,113	771,883
Net earnings	—	—	—	—	75,202	75,202
Reclassification of gain on swap extinguishment	—	—	(1,167)	—	—	(1,167)
Change in net unrealized loss on swaps used in cash flow hedges	—	—	(1,874)	—	—	(1,874)
Change in net unrealized gain on securities available for sale	—	—	389	—	—	389
Total comprehensive income	—	—	—	—	—	72,550
Stock options exercised	4	2,201	—	—	—	2,205
Stock-based compensation	—	2,718	—	—	—	2,718
Tax benefit from stock-based compensation	—	1,000	—	—	—	1,000
Dividends paid ($0.60 per share)	—	—	—	—	(38,122)	(38,122)
Balance at December 31, 2006	636	63,223	5,182	—	743,193	812,234
Net loss	—	—	—	—	(39,225)	(39,225)
Reclassification of gain on swap extinguishment	—	—	(101)	—	—	(101)
Change in net unrealized loss on swaps used in cash flow hedges	—	—	(3,957)	—	—	(3,957)
Change in net unrealized loss on securities available for sale	—	—	(12,619)	—	—	(12,619)
Total comprehensive loss	—	—	—	—	—	(55,902)
Adjustment to initially apply FIN 48	—	—	—	—	(1,428)	(1,428)
Stock options exercised	1	69	—	—	—	70
Stock-based compensation	—	1,083	—	—	—	1,083
Tax effect from stock-based compensation	—	(25)	—	—	—	(25)
Purchase of treasury stock	—	—	—	(41,705)	—	(41,705)
Issuance of treasury stock	—	—	—	26	—	26
Dividends paid ($0.35 per share)	—	—	—	—	(21,375)	(21,375)
Balance at December 31, 2007	$637	$64,350	$(11,495)	$(41,679)	$681,165	$692,978

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

Flagstar Bancorp, Inc.
Consolidated Statements of Cash Flows
(In thousands)

	For the Years Ended December 31,		
	2007	2006	2005
Operating Activities			
Net (loss) earnings	$ (39,225)	$ 75,202	$ 79,865
Adjustments to net (loss) earnings to net cash (used in) provided by operating activities			
Provision for loan losses	88,297	25,450	18,876
Depreciation and amortization	102,965	100,710	125,978
(Decrease) increase in valuation allowance in mortgage servicing rights	(428)	599	—
FHLB stock dividends	—	—	(5,035)
Stock-based compensation expense	1,083	2,718	745
Net gain on the sale of assets	(3,230)	(2,328)	(1,623)
Net gain on loan sales	(59,030)	(42,381)	(63,580)
Net gain on sales of mortgage servicing rights	(5,898)	(92,621)	(18,157)
Net loss on securities available for sale	16,679	6,163	—
Loss on trading securities	6,785	—	—
Proceeds from sales of loans available for sale	22,939,708	15,018,393	22,985,540
Origination and repurchase of mortgage loans available for sale, net of principal repayments	(24,131,163)	(15,786,616)	(22,538,139)
Increase in accrued interest receivable	(5,130)	(4,359)	(13,352)
Decrease (increase) in other assets	(18,130)	66,348	45,379
Increase in accrued interest payable	768	5,014	13,143
Net tax effect of (benefit for) stock grants issued	25	(1,000)	—
Increase (decrease) liability for checks issued	(10,658)	(1,599)	4,281
(Decrease) increase in federal income taxes payable	(40,301)	(44,367)	49,696
(Decrease) increase in payable for securities purchased	(249,694)	249,694	—
(Decrease) increase in other liabilities	2,533	(4,814)	(16,656)
Net cash (used in) provided by operating activities	(1,404,044)	(429,794)	666,961
Investing Activities			
Net change in other investments	(2,778)	(2,078)	(3,566)
Repayment of mortgage-backed securities held to maturity	336,836	404,073	71,478
Purchase of mortgage-backed securities held to maturity	—	(118,025)	—
Proceeds from the sale of investment securities available for sale	573,143		
Purchase of investment securities available for sale	(108,259)	(574,999)	—
Proceeds from sales of portfolio loans	694,924	1,329,032	452,949
Origination of portfolio loans, net of principal repayments	(677,058)	(1,086,596)	(3,008,219)
Purchase of Federal Home Loan Bank stock	(71,374)	(6,762)	(52,238)
Redemption of Federal Home Loan Bank stock	—	21,310	—
Investment in unconsolidated subsidiaries	1,238	—	3,095
Proceeds from the disposition of repossessed assets	89,571	52,812	39,078
Acquisitions of premises and equipment, net of proceeds	(38,734)	(45,493)	(51,337)
Proceeds from the sale of mortgage servicing rights	33,632	388,784	124,860
Net cash provided by (used in) investing activities	831,141	362,058	(2,423,900)
Financing Activities			
Net (decrease) increase in deposit accounts	613,256	(898,268)	1,087,980
Net (decrease) increase in security repurchase agreements	(882,806)	(69,291)	1,060,097
Issuance of junior subordinated debt	40,000	—	100,000
Net increase in Federal Home Loan Bank advances	894,000	1,182,000	135,000
Payment on other long term debt	(25)	(25)	(25)
Net (disbursement) receipt of payments of loans serviced for others	35,020	(34,487)	(427,561)
Net (disbursement) receipt of escrow payments	(600)	(1,203)	(125,659)
Proceeds from the exercise of stock options	70	2,205	7,444
Net tax effect (benefit for) stock grants issued	(25)	1,000	8,379
Dividends paid to stockholders	(21,375)	(38,122)	(55,995)
Purchase of treasury stock	(41,705)	—	—
Issuance of treasury stock	26	—	—
Net cash provided by financing activities	635,836	143,809	1,789,660
Net increase in cash and cash equivalents	62,933	76,073	32,721
Beginning cash and cash equivalents	277,236	201,163	168,442
Ending cash and cash equivalents	$ 340,169	$ 277,236	$ 201,163
Supplemental disclosure of cash flow information:			
Loans held for investment transferred to repossessed assets	$ 144,824	$ 102,446	$ 47,416
Total interest payments made on deposits and other borrowings	$ 694,863	$ 580,905	$ 449,250
Federal income taxes paid	$ —	$ 86,953	$ —
Recharacterization of mortgage loans held for investment to mortgage-backed securities held to maturity	$ 345,659	$ 558,732	$ 1,466,477
Recharacterization of mortgage loans available for sale to mortgage-backed securities available for sale	$ 848,780	$ —	$ —
Reclassification of mortgage loans originated for portfolio to mortgage loans available for sale	$ 694,924	$ 1,329,032	$ 452,949
Reclassification of mortgage loans originated available for sale then transferred to portfolio loans	$ 1,394,227	$ 354,662	$ 883,119
Mortgage servicing rights resulting from sale or securitization of loans	$ 346,348	$ 223,934	$ 328,954
Retention of residual interests in securitization transactions	$ 20,487	$ 22,466	$ 26,148

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

Flagstar Bancorp, Inc.
Notes to the Consolidated Financial Statements

Note 1 — Nature of Business

Flagstar Bancorp, Inc. ("Flagstar" or the "Company"), is the holding company for Flagstar Bank, FSB (the "Bank"), a federally chartered stock savings bank founded in 1987. With $15.8 billion in assets at December 31, 2007, Flagstar is the largest savings institution and banking institution headquartered in Michigan.

The Company's principal business is obtaining funds in the form of deposits and wholesale borrowings and investing those funds in single-family mortgages and other types of loans. Its primary lending activity is the acquisition or origination of single-family mortgage loans. The Company also originates consumer loans, commercial real estate loans, and non-real estate commercial loans and services a significant volume of residential mortgage loans for others.

The Company sells or securitizes most of the mortgage loans that it originates and generally retains the right to service the mortgage loans that it sells. These mortgage-servicing rights ("MSRs") are occasionally sold by the Company in transactions separate from the sale of the underlying mortgages. The Company may also invest in a significant amount of its loan production in order to enhance the Company's leverage ability and to receive the interest spread between earning assets and paying liabilities.

The Bank is a member of the Federal Home Loan Bank System ("FHLB") and is subject to regulation, examination and supervision by the Office of Thrift Supervision ("OTS") and the Federal Deposit Insurance Corporation ("FDIC"). The Bank's deposits are insured by the FDIC through the Deposit Insurance Fund ("DIF").

Note 2 — Summary of Significant Accounting Policies

The following significant accounting policies of the Company, which are applied in the preparation of the accompanying consolidated financial statements, conform to accounting principles generally accepted in the United States of America ("U.S. GAAP").

Basis of Presentation and Consolidation

The consolidated financial statements include the accounts of the Company and its consolidated subsidiaries. All significant intercompany balances and transactions have been eliminated. In accordance with current accounting principles, our trust subsidiaries are not consolidated. Certain prior period amounts have been reclassified to conform to the current period presentation.

Accounting Research Bulletin 51 ("ARB 51"), *Consolidated Financial Statements,* requires a company's consolidated financial statements to include subsidiaries in which the company has a controlling financial interest. This requirement usually has been applied to subsidiaries in which a company has a majority voting interest. Currently, all of the Company's subsidiaries are wholly-owned.

The voting interest approach defined in ARB 51 is not applicable in identifying controlling financial interests in entities that are not controllable through voting interests or in which the equity investors do not bear the residual economic risks. In such instances, Financial Accounting Standards Board Interpretation 46 ("FIN 46"), *Consolidation of Variable Interest Entities* ("VIE") and FIN 46R — "Implicit Variable Interests under FIN 46, Consolidation of Variable Interest Entities," provide guidance on when a company should include in its financial statements the assets, liabilities, and activities of another entity. In general, a VIE is a corporation, partnership, trust, or any other legal structure used for business purposes that either does not have equity investors with voting rights or has equity investors that do not provide sufficient financial resources for the entity to support its activities. FIN 46R requires a VIE to be consolidated by a company if that company is subject to a majority of the risk of loss from the VIE's activities or entitles it to receive a majority of the entity's residual returns or both. A company that consolidates a VIE is called the primary beneficiary of that entity. The Company has no consolidated VIEs.

The Company uses special-purpose entities ("SPEs"), primarily securitization trusts, to diversify its funding sources. SPEs are not operating entities, generally have no employees, and usually have a limited life. The basic SPE structure involves the Bank transferring assets to the SPE. The SPE funds the purchase of those assets by issuing asset-backed securities to investors. The legal documents governing the SPE describe how the cash received on the assets held in the SPE must be allocated to the investors and other parties that have rights to these cash flows.

The Bank structures these SPEs to be bankruptcy remote, thereby insulating investors from the impact of the creditors of other entities, including the transferor of the assets.

Where the Bank is a transferor of assets to an SPE, the assets sold to the SPE generally are no longer recorded on the statement of financial condition and the SPE is not consolidated when the SPE is a qualifying special-purpose entity ("QSPE"). Statement of Financial Accounting Standards ("SFAS") 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* provides specific criteria for determining when an SPE meets the definition of a QSPE. In determining whether to consolidate non-qualifying SPEs where assets are legally isolated from the Bank's creditors, the Company considers such factors as the amount of third-party equity, the retention of risks and rewards, and the extent of control available to third parties. The Bank currently services certain home equity loans and lines that were sold to securitization trusts.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could materially differ from those estimates.

Cash and Cash Equivalents

Cash on hand, cash items in the process of collection, and amounts due from correspondent banks and the Federal Reserve Bank are included in cash and cash equivalents and overnight deposits.

Securities

Investments in debt securities and certain equity securities with readily determinable fair values are accounted for under SFAS 115, *Accounting for Certain Investments in Debt and Equity Securities*. SFAS 115 requires investments to be classified within one of three categories, trading, held to maturity or available for sale based on the type of security and management's intent with regards to selling the security.

Trading securities represent non-investment grade residual interests from the 2007 private-label securitization. These securities are recorded at fair value with any unrealized gains or losses reported in the consolidated statement of operations.

Securities available for sale are carried at fair value with unrealized gains and losses deemed to be temporary being reported in other comprehensive income (loss), net of tax. Any gains or losses realized upon the sale of a security or unrealized losses that are deemed to be other-than-temporary are reported in the consolidated statement of operations. The securities available for sale represent certain mortgage-backed securities and certain non-investment grade residual interests in the Company's private securitizations completed prior to 2007.

Certain mortgage-backed securities are classified as held to maturity because management has the positive intent and ability to hold these securities to maturity. Securities held to maturity are carried at amortized cost. Unrealized losses that are deemed to be other-than-temporary are reported in the consolidated statement of operations.

Other investments, which include certain investments in mutual funds that by their nature cannot be held to maturity, are carried at fair value. Increases or decreases in fair value are recorded in the statement of consolidated operations.

Interest on securities, including the amortization of premiums and the accretion of discounts using the effective interest method over the period of maturity, is included in interest income. Realized gains and losses on the sale of securities and other-than-temporary impairment charges on securities are determined using the specific-identification method.

Loans

Loans are designated as held for investment or available for sale or securitization during the origination process. Loans held for investment are carried at amortized cost. The Company has both the intent and the ability to hold all loans held for investment for the foreseeable future. Loans available for sale are carried at the lower of aggregate cost or estimated market value. Loans are stated net of deferred loan origination fees or costs. Interest income on loans is recognized on the accrual basis based on the principal balance outstanding. Loan origination fees and direct origination costs associated with loans are deferred and amortized over the expected life of the loans as an adjustment to the yield using the interest method. Net unrealized losses on loans available for sale are recognized in a valuation allowance that is charged to operations. Gains or losses recognized upon the sale of loans are determined using the specific identification method. When loans originally designated as available for sale or loans originally designated as held for investment are reclassified, cash flows associated with the loans will be classified in the consolidated cash flow statement as operating or investing, as appropriate, in accordance with the initial classification of the loans.

Delinquent Loans

Loans are placed on non-accrual status when any portion of principal or interest is 90 days delinquent, or earlier when concerns exist as to the ultimate collection of principal or interest. When a loan is placed on non-accrual status, the accrued and unpaid interest is reversed and interest income is recorded as collected. Loans return to accrual status when principal and interest become current and are anticipated to be fully collectible.

Loan Sales and Securitizations

Our recognition of gain or loss on the sale or securitization of loans is accounted for in accordance with SFAS 140. SFAS 140 requires that a transfer of financial assets in which we surrender control over the assets be accounted for as a sale to the extent that consideration other than beneficial interests in the transferred assets is received in exchange. The carrying value of the assets sold is allocated between the assets sold and the retained interests, other than the mortgage servicing rights, based on their relative fair values. Retained mortgage servicing rights are recorded at fair value.

SFAS 140 requires, for certain transactions, a “true sale” analysis of the treatment of the transfer under state law if the company was a debtor under the bankruptcy code. The “true sale” analysis includes several legal factors including the nature and level of recourse to the transferor and the nature of retained servicing rights. The “true sale” analysis is not absolute and unconditional but rather contains provisions that make the transferor “bankruptcy remote”. Once the legal isolation of financial assets has been met and is satisfied under SFAS 140, other factors concerning the nature of the extent of the transferor’s control over the transferred financial assets are taken into account in order to determine if the de-recognition of financial assets is warranted, including whether the special purpose entity (“SPE”) has complied with rules concerning qualifying special purpose entities.

The Bank is not eligible to become a debtor under the bankruptcy code. Instead, the insolvency of the Bank is generally governed by the relevant provisions of the Federal Deposit Insurance Act and the FDIC’s regulations. However, the "true sale" legal analysis with respect to the Bank is similar to the "true sale" analysis that would be done if the Bank were subject to the bankruptcy code.

The Bank obtains a legal opinion regarding the legal isolation of the transferred financial assets as part of the securitization process. The "true sale" opinion provides reasonable assurance that the transferred assets would not be characterized as property of the transferor in the event of insolvency and also states that the transferor would not be required to substantively consolidate the assets and liabilities of the purchaser SPE with those of the transferor upon such event.

The securitization process involves the sale of loans to our wholly-owned bankruptcy remote special purpose entity which then sells the loans to a separate, transaction-specific trust in exchange for considerations generated by the sale of the securities issued by the securitization trust. The securitization trust issues and sells debt securities to third party investors that are secured by payments on the loans. We have no obligation to provide credit support to either the third party investors or the securitization trust. Neither the third party investors nor the securitization trust generally have recourse to our assets or us and have no ability to require us to repurchase their securities other than through enforcement of the standard representations and warranties. We do make certain representations and warranties concerning the loans, such as lien status, and if we are found to have breached a representation and warranty, we may be required to repurchase the loan from the securitization trust. We do not guarantee any securities issued by the securitization trust. The securitization trust represents a "qualifying special purpose entity", which meets the certain criteria of SFAS 140, and therefore is not consolidated for financial reporting purposes.

In addition to the cash we receive from the sale or securitization of loans, we retain certain interests in the securitized assets. The retained interests include mortgage servicing rights ("MSR's") and a residual interest. The residuals are included in securities available for sale or trading securities on the consolidated statement of financial condition.

We retain the servicing function for securitized loans. As a servicer, we are entitled to receive a servicing fee equal to a specified percentage of the outstanding principal balance of the loans. We may also be entitled to receive additional servicing compensation, such as late payment fees.

Transaction costs associated with the securitization process are recognized as a component of the gain or loss at the time of sale.

Allowance for Loan Losses

The allowance for loan losses represents management's estimate of probable losses inherent in the Company's loans held for investment portfolio as of the date of the consolidated financial statements. The allowance provides for probable losses that have been identified with specific customer relationships and for probable losses believed to be inherent in the loan portfolio but that have not been specifically identified.

The Company performs a detailed credit quality review at least annually on large commercial loans as well as selected other smaller balance commercial loans and may allocate a specific portion of the allowance to such loans based upon this review. Commercial and commercial real estate loans that are determined to be substandard and exceed $1.0 million are treated as impaired and given an individual evaluation to determine the necessity of a specific reserve in accordance with the provisions of SFAS 114, *Accounting by Creditors for Impairment of a Loan.* This pronouncement requires an allowance to be established as a component of the allowance for loan losses when it is probable that all amounts due will not be collected pursuant to the contractual terms of the loan and the recorded investment in the loan exceeds its fair value. Fair value is measured using either the present value of the expected future cash flows discounted at the loan's effective interest rate, the observable market price of the loan, or the fair value of the collateral if the loan is collateral dependent, reduced by estimated disposal costs. In estimating the fair value of collateral, we typically utilize outside fee-based appraisers to evaluate various factors such as occupancy and rental rates in our real estate markets and the level of obsolescence that may exist on assets acquired from commercial business loans.

A portion of the allowance is allocated to the remaining commercial loans by applying projected loss ratios, based on numerous factors identified below, to the loans within the different risk ratings.

Additionally, management has sub-divided the homogeneous portfolios, including consumer and residential mortgage loans, into categories that have exhibited greater loss exposure (such as sub-prime loans and loans that are not salable on the secondary market because of collateral or documentation issues). The portion of the allowance allocated to other consumer and residential mortgage loans is determined by applying projected loss ratios to various segments of the loan portfolio. Projected loss ratios incorporate factors such as recent charge-off experience, current economic conditions and trends, and trends with respect to past due and nonaccrual amounts, and are supported by underlying analysis.

Management maintains an unallocated allowance to recognize the uncertainty and imprecision underlying the process of estimating expected loan losses.

As the process for determining the adequacy of the allowance requires subjective and complex judgment by management about the effect of matters that are inherently uncertain, subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for loan losses. In estimating the amount of credit losses inherent in the Company's loan portfolio, various assumptions are made. For example, when assessing the condition of the overall economic environment, assumptions are made regarding current economic trends and their impact on the loan portfolio. In the event the national economy were to sustain a prolonged downturn, the loss factors applied to our portfolios may need to be revised, which may significantly impact the measurement of the allowance for loan losses. For impaired loans that are collateral dependent, the estimated fair value of the collateral may deviate significantly from the proceeds received when the collateral is sold.

Repossessed Assets

Repossessed assets include one-to-four family residential property, commercial property, and one-to-four family homes under construction that were acquired through foreclosure. Repossessed assets are initially recorded at estimated fair value, less estimated selling costs. Subsequently, properties are evaluated and any additional declines in value are recorded in current period earnings. The amount the Company ultimately recovers on repossessed assets may differ substantially from the net carrying value of these assets because of future market factors beyond the Company's control.

Federal Home Loan Bank Stock

The Bank owns stock in the Federal Home Loan Bank ("FHLB"). No ready market exists for the stock and it has no quoted market value. The stock is redeemable at par and is carried at cost. The investment is required to permit the Bank to borrow from the Federal Home Loan Bank of Indianapolis ("FHLBI").

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Land is carried at historical cost. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets as follows:

Office buildings — 31.5 years
Computer hardware and software — 3 to 5 years
Furniture, fixtures and equipment — 5 to 7 years
Automobiles — 3 years

Repairs and maintenance costs are expensed in the period they are incurred, unless they are covered by a maintenance contract, which is expensed equally over the stated term of the contract. Repairs and maintenance costs are included as part of occupancy and equipment expenses.

Mortgage Servicing Rights

In March 2006, FASB issued SFAS 156*, Accounting for Servicing of Financial Assets an amendment of FASB Statement 140*. SFAS 156 requires an entity to recognize a servicing asset or liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract. It requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value and permits an entity to choose either an amortization or fair value measurement method for each class of separately recognized servicing assets and servicing liabilities. Effective January 1, 2006, the Company adopted SFAS 156, as permitted. Adoption of this pronouncement allowed the Company to initially recognize its MSRs at fair value. The Company elected to retain the amortization method for subsequently accounting for the MSRs.

The Company purchases and originates mortgage loans for sale to the secondary market and sells the loans on either a servicing-retained or servicing-released basis. MSRs are recognized as assets at the time a loan is sold on a servicing-retained basis. The capitalized cost of retained MSRs is amortized in proportion to, and over the period of, estimated net future servicing revenue. The expected period of the estimated net servicing income is based, in part, on the expected prepayment period of the underlying mortgages.

MSRs are periodically evaluated for impairment. For purposes of measuring impairment, MSRs are stratified based on predominant risk characteristics of the underlying serviced loans. These risk characteristics include loan type (fixed or adjustable rate), term (15 year, 20 year, 30 year or balloon) and interest rate. Impairment represents the excess of amortized cost of an individual stratum over its estimated fair value, and is recognized through a valuation allowance.

Fair values for individual stratum are based on the present value of estimated future cash flows using a discount rate commensurate with the risks involved. Estimates of fair value include assumptions about prepayment, default and interest rates, and other factors, which are subject to change over time. Changes in these underlying assumptions could cause the fair value of MSRs, and the related valuation allowance, to change significantly in the future.

The Company occasionally sells a certain portion of its MSRs to investors. At the time of the sale the Company records a gain or loss on such sale based on the selling price of the MSRs less the carrying value and transaction costs. The MSRs are sold in separate transactions from the sale of the underlying loans.

Financial Instruments and Derivatives

In seeking to protect its financial assets and liabilities from the effects of changes in market interest rates, the Company has devised and implemented an asset/liability management strategy that seeks, on an economic and accounting basis, to mitigate significant fluctuations in our financial position and results of operations. Loans held for investment generate interest income and MSRs generate fee income. With regard to the pipeline of mortgage loans held for sale, in general, the Company hedges these assets with forward commitments to sell Fannie Mae or Freddie Mac securities with comparable maturities and weighted- average interest rates. Further, the Company occasionally enters into swap agreements to hedge the cash flows on certain liabilities.

SFAS 133, *Accounting for Derivative Instruments and Hedging Activities,* as amended and interpreted, requires that we recognize all derivative instruments on the statement of financial condition at fair value. If certain conditions are met, special hedge accounting may be applied and the derivative instrument may be specifically designated as:

(a) a hedge of the exposure to changes in the fair value of a recognized asset, liability or unrecognized firm commitment, referred to as a fair value hedge, or

(b) a hedge of the exposure to the variability of cash flows of a recognized asset, liability or forecasted transaction, referred to as a cash flow hedge.

In the case of a qualifying fair value hedge, changes in the value of the derivative instruments that are highly effective (as defined in SFAS 133) are recognized in current earnings along with the changes in value of the designated hedged item. In the case of a qualifying cash flow hedge, changes in the value of the derivative instruments that are highly effective are recognized in accumulated other comprehensive income ("OCI"), until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value is recognized through earnings. Upon the occasional termination of a cash flow hedge, the remaining cost of the hedge is amortized over the remaining life of the hedged item in proportion to the change in the hedged forecasted transaction. The Company has derivatives in place to hedge the exposure to the variability in future cash flows for forecasted transactions. Derivatives that are non-designated hedges, as defined in SFAS 133 are adjusted to fair value through operations. The Company formally documents all qualifying hedge relationships, as well as the risk management objective and strategy for undertaking each hedge transaction. The Company is not a party to any foreign currency hedge relationships. During the fourth quarter of 2005, the Company derecognized all fair value hedges and has no fair value hedges outstanding subsequently. On January 1, 2008, the Company derecognized all cash flow hedges.

Security Repurchase Agreements

Securities sold under agreements to repurchase are generally accounted for as collateralized financing transactions and are recorded at the amounts at which the securities were sold plus accrued interest. Securities, generally mortgage-backed securities, are pledged as collateral under these financing arrangements. The fair value of collateral provided to a party is continually monitored and additional collateral is obtained or requested to be returned, as appropriate.

Trust Preferred Securities

As of December 31, 2007, the Company sponsored eight trusts, of which 100% of the common equity is owned by the Company. Each of the trusts has issued trust preferred securities to third party investors and loaned the proceeds to the Company in the form of junior subordinated notes, which are included in long term debt in these consolidated financial statements. The notes held by each trust are the sole assets of that trust. Distributions on the trust preferred securities of each trust are payable quarterly at a rate equal to the interest being earned by the trust on the notes held by these trusts.

The trust preferred securities are subject to mandatory redemption upon repayment of the notes. The Company has entered into agreements which, taken collectively, fully and unconditionally guarantee the trust preferred securities subject to the terms of each of the guarantees. The securities are not subject to a sinking fund requirement and are not convertible into any other securities of the Company. The Company has the right to defer dividend payments to the trust preferred security holders for up to five years.

The trusts are VIEs under U.S. GAAP (i.e., FIN 46R) and are not consolidated. The Company's investment in the common stock of these trusts is included in other assets in the Company's consolidated statement of financial condition. The trust preferred securities held by the trusts qualify as Tier 1 capital under current banking regulations.

Income Taxes

The Company accounts for income taxes on the asset and liability method. Deferred tax assets and liabilities are recorded based on the difference between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Current taxes are measured by applying the provisions of enacted tax laws to taxable income to determine the amount of taxes receivable or payable. The Company files a consolidated federal income tax return on a calendar year basis.

In June 2006, the FASB issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement 109,* ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with SFAS 109, *Accounting for Income Taxes.* This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 was adopted by the Company on January 1, 2007, which is described more fully in Note 16.

Secondary Market Reserve

The Company sells or securitizes most of the residential mortgage loans that it originates into the secondary mortgage market. When the Company sells mortgage loans it makes customary representations and warranties to the purchasers about various characteristics of each loan, such as the manner of origination, the nature and extent of underwriting standards applied and the types of documentation being provided. Typically these representations and warranties are in place for the life of the loan. If a defect in the origination process is identified, the Company may be required to either repurchase the loan or indemnify the purchaser for losses it sustains on the loan. If there are no such defects, the Company has no liability to the purchaser for losses it may incur on such loan. The Company maintains a secondary market reserve to account for the expected losses related to loans it might be required to repurchase (or the indemnity payments it may have to make to purchasers). The secondary market reserve takes into account both our estimate of expected losses on loans sold during the current accounting period, as well as adjustments to the Company's previous estimates of expected losses on loans sold. In each case these estimates are based on the Company's most recent data regarding loan repurchases and indemnifications, actual credit losses on repurchased and indemnified loans and recovery history, among other factors. Increases to the secondary market reserve for current loan sales reduce the Company's net gain on loan sales. Adjustments to the Company's previous estimates are recorded as an increase or decrease in other fees and charges.

Advertising Costs

Advertising costs are expensed in the period they are incurred and are included as part of general and administrative expenses. Advertising expenses totaled $10.3 million, $9.4 million, and $7.5 million for the years ended December 31, 2007, 2006 and 2005, respectively.

Stock-Based Compensation

On January 1, 2006, the Company adopted SFAS 123R, *Accounting for Stock-Based Compensation* ("SFAS 123R"). SFAS 123R requires all share-based payment to employees, including grants of employee stock options, to be recognized as expense in the statement of operations based on their fair values. Prior to SFAS 123R, only certain pro forma disclosures of fair value were required. The amount of compensation is measured at the fair value of the options when granted and this cost is expensed over the required service period, which is normally the vesting period of the options. SFAS 123R applies to awards granted or modified after January 1, 2006 or any unvested awards outstanding at December 31, 2005. The effect of the adoption of the new accounting principle on results of operations depends on the level of option grants, the vesting period for those grants, and the fair value of the options granted at such date. Existing options that vested after the adoption date resulted in additional compensation expense of approximately $0.1 million in 2007 and $1.2 million in 2006. The Company utilized the disclosure requirements permitted by SFAS 123, *Accounting for Stock-Based Compensation* ("SFAS 123"), for transactions entered into during 1996 and through December 31, 2005. For the periods prior to January 1, 2006, the Company elected to remain with the former method of accounting under *Accounting Principles Board Opinion 25* ("APB 25") and has made the pro forma disclosures in Note 28 of net earnings and earnings per share as if the fair value method provided for in SFAS 123 had been adopted.

At December 31, 2007, the Company has a stock-based employee compensation plan, which is described more fully in Note 28.

Recently Issued Accounting Standards

In September 2006, the FASB issued SFAS 157 *Fair Value Measurements.* SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with U.S. GAAP, and expands disclosures about fair value measurements. SFAS 157 clarifies that the exchange price is the price in an orderly transaction between market participants to sell an asset or transfer a liability at the measurement date. SFAS 157 emphasizes that fair value is a market-based measurement and not an entity-specific measurement. It also establishes a fair value hierarchy used in fair value measurements and expands the required disclosures of assets and liabilities measured at fair value. The Company will be required to adopt this statement beginning in 2008. See Note 3, "Fair Value Accounting" for further information.

In September 2006, the FASB issued SFAS 158 *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans.* SFAS 158 amends SFAS Statements 87, 88, 106 and 132(R). SFAS 158 requires employers to recognize in their statement of financial position an asset for a plan's overfunded status or a liability for a plan's underfunded status. Secondly, it requires employers to measure the plans assets and obligations that determine its funded status as of the end of the fiscal year. Lastly, employers are required to recognize changes in the funded status of a defined benefit postretirement plan in the year that the changes occur with the changes reported in comprehensive income. SFAS 158 is required to be adopted by entities having fiscal years ending after December 15, 2006. Because the Company does not have any defined benefit plans or other post retirement plans this standard did not have an impact on the Company's financial condition, results of operation or liquidity.

In February 2007, the FASB issued SFAS 159 *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS 159 permits entities to choose to measure financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The decision to elect the fair value option may be applied instrument by instrument, is irrevocable and is applied to the entire instrument and not to only specified risks, specific cash flows or portions of that instrument. An entity is restricted in choosing the dates to elect the fair value option for an eligible item. Adoption of SFAS 159 is effective for the Company on January 1, 2008. See Note 3, "Fair Value Accounting" for further information.

In November 2007, the FASB issued SFAS 160 *Non-controlling Interest in Consolidated Financial Statements — an amendment to ARB No. 51.* SFAS 160 changes the way consolidated net earnings are presented. The new standard requires consolidated net earnings to be reported at amounts attributable to both the parent and the non-controlling interest and will require disclosure on the face of the consolidated statement of income amounts attributable to the parent and the non-controlling interest. The adoption of this statement will result in more transparent reporting of the net earnings attributable to non-controlling interest. The statement establishes a single method of accounting for changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation. The statement also requires that a parent recognize a gain or loss in net earnings when a subsidiary is deconsolidated. The adoption of SFAS 160 is effective for the Company on

January 1, 2009. Management does not expect that the adoption of this statement will have a material impact on the Company's financial condition, results of operation or liquidity.

In November 2007, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin 109 ("SAB 109"). SAB 109 expresses the views of the SEC regarding the written loan commitments that are accounted for at fair value through earnings under generally accepted accounting principles. SAB 109 supersedes SAB 105 and expresses the current view of the staff that, consistent with the guidance in SFAS 156 *Accounting for Servicing of Financial Assets* and SFAS 159 *The Fair Value Option for Financial Assets and Financial Liabilities*, the expected net future cash flows related to the associated servicing of the loans should be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. The adoption of SAB 109 is effective on a prospective basis for the Company's derivative loan commitments issued or modified on January 1, 2008. See Note 3 — Fair Value Accounting for further information.

In December 2007, the SEC issued Staff Accounting Bulletin 110 ("SAB 110"). SAB 110 expresses the views of the SEC regarding the use of a "simplified" method in developing an estimate of expected term of "plain vanilla" share options as discussed in SAB 107 and issued under SFAS 123 (revised 2004), *Share-Based Payment*. The SEC indicated in SAB 107 that it would accept a company's decision to use the simplified method, regardless of whether the company has sufficient information to make more refined estimates of expected term. Under SAB 107, the SEC had believed detailed information about employee exercise behavior would be readily available and therefore would not expect companies to use the simplified method for share option grants after December 31, 2007. SAB 110 states that the SEC will continue to accept, under certain circumstances, the use of the simplified method beyond December 31, 2007. Because the Company does not utilize the simplified method, management does not expect that this pronouncement will have a material impact on the Company's financial condition, results of operation or liquidity.

Note 3. Fair Value Accounting

On January 1, 2008, the Company was required to adopt SFAS 157 and SFAS 159. SFAS 157 establishes a framework for measuring fair value and expands disclosure requirements. Specifically, SFAS 157 emphasizes that fair value is market based and not entity specific. The pronouncement clarifies that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at a measurement date. Further, a fair value hierarchy is established which prioritizes the three broad categories of inputs that might be used in valuation determinations. The highest priority in the fair value hierarchy is quoted prices (unadjusted) available in active markets for identical assets or liabilities (Level 1). The second priority (Level 2) in the hierarchy is other than quoted prices in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (for example, interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks, and default rates.) Level 3 inputs are unobservable inputs for the asset or liability. There is typically little, if any, market activity for the asset or liability. However, the fair value measurement objective remains the same, that is, an exit price from the perspective of a market participant. Valuations determined utilizing primarily Level 3 inputs are generally supported by internal valuation models.

The adoption of SFAS 157 as of January 1, 2008 is not expected to have a material impact on the Company's financial condition, operations or cash flows. The adoption of SFAS 157 will require additional disclosures with respect to our fair value asset and liabilities and the hierarchy in which the valuation of each was determined.

At December 31, 2007, $1.7 billion of the Company's assets and none of its liabilities were carried at fair value. Of the assets carried at fair value, $47.0 million were determined using principally Level 3 inputs.

Additionally, the Company's MSRs are recorded at fair value at creation but are accounted for using the amortization method thereafter, being measured for impairment periodically.

SFAS 159, which was also adopted as of January 1, 2008, allows entities to elect to measure those financial instruments and certain other items at fair value that are not currently required to be measured at fair value. This election may be applied on an instrument by instrument basis, is irrevocable once made and must be applied to the entire instrument and not to specified risks, specific cash flows or other limited aspects of that instrument. The entity is also restricted in choosing the dates to elect the fair value option for eligible items.

In accordance with the provisions of SFAS 159, the Company, as of January 1, 2008, elected to adopt the fair value option for its residual interests previously carried as available for sale securities. As such, these securities will be reclassified to trading securities. At January 1, 2008, there was no amount in accumulated other comprehensive income (loss) that was required to be recorded as an increase or decrease to beginning retained earnings in 2008 as a result of this election.

Also as of January 1, 2008, the Company adopted SAB 109 which superseded SAB 105 and, in conjunction with SFAS 157 and 159, allows entities to recognize the expected net future cash flows associated with servicing of the loans for all written loan commitments that are accounted for at fair value (i.e. — derivatives). This pronouncement was adopted on a prospective basis.

Note 4. Investment Securities

As of December 31, 2007 and 2006, investment securities were comprised of the following (dollars in thousands):

	December 31, 2007	December 31, 2006
Securities — trading	$ 13,703	$ —
Securities — available for sale		
AAA-rated non-agencies	$ 821,245	$ 497,089
AAA-rated U.S. government sponsored agencies	454,030	77,910
Non-investment grade residual	33,333	42,451
Total mortgage-backed securities — available for sale	$1,308,608	$ 617,450
Mortgage-backed securities — held to maturity		
AAA-rated non-agencies	$ —	$ 332,362
AAA-rated U.S. government sponsored agencies	1,255,431	1,233,058
Total mortgage-backed securities — held to maturity	$1,255,431	$1,565,420
Other investments		
Mutual funds	$ 26,107	$ 23,320
U.S. Treasury bonds	706	715
Total other investments	$ 26,813	$ 24,035

At December 31, 2007, the Company had $13.7 million in securities classified as trading. These securities are non-investment grade residual securities from a private-label securitization that was closed in March 2007 with a secondary closing in June 2007. The securities are recorded at fair value with any unrealized gains and losses reported in the consolidated statement of operations. Prior to this transaction, the Company had no securities classified as trading. During 2007, the Company recognized losses related to these trading securities of $6.8 million as a result of the decrease in the fair value of the securities. The decline in the fair value of these residual securities was principally due to the increase in the expected losses in the second mortgages that underly this asset.

At December 31, 2007, the Company had $1.3 billion in securities classified as available for sale, which were comprised of AAA-rated non-agency securities, AAA-rated U.S. government sponsored agency securities and non-investment grade residual securities arising from certain of its private-label securitizations. Securities available for sale are carried at fair value, with unrealized gains and losses reported as a component of other comprehensive (loss) income to the extent they are temporary in nature. If losses are, at any time, deemed to have arisen from "other-than-temporary impairments" (OTTI), then they are reported as an expense for that period. At December 31, 2007, $570.0 million of the securities classified as available for sale were pledged as collateral for security repurchase agreements as well as for FHLB advances. Contractual maturities of the securities generally range from 2035 to 2037. Expected weighted average lives of these securities generally range from several months to 6 years due to borrower prepayments occurring prior to the contractual maturity.

During the quarter ended March 31, 2007, the Company received written guidance from the OTS on regulatory capital treatment being used by the Bank for securities retained from a guaranteed mortgage securitization of fixed second mortgage loans completed in April 2006. The securities had initially been recorded as held to maturity because the underlying bonds were AAA-rated and insured by a private insurance company and, therefore, the Bank expected that the securities would receive 20% risk-weighted capital treatment rather than 50% or 100% risk-weighted treatment. At the time, the Company had both the ability and intent to hold the securities to maturity. In its guidance, the OTS advised the Company that the recharacterization of the underlying loans in the guaranteed mortgage securitization did not decrease the risk associated with carrying fixed second mortgage loans because the capital rules did not recognize private insurance companies as eligible guarantors. Because of this information received from the OTS, the Company's capital treatment of the underlying securities changed significantly. As a result, the Company no longer intends to hold the securities to maturity and during the quarter ended March 31, 2007, reclassified $321.1 million in securities associated with the guaranteed mortgage securitization of fixed second mortgage loans completed in April 2006 to securities available for sale. Upon reclassification of the securities to available for sale, the Company recorded a $1.3 million loss, before taxes, to other comprehensive income. Management does not believe that this capital treatment could have been reasonably anticipated and the reclassification to available for sale should not impact the held to maturity status of the Company's other held to maturity securities. At December 31, 2007, the Company had $1.3 billion in AAA-rated mortgage-backed securities classified as held to maturity. Of such securities, $107.3 million were pledged as collateral for security repurchase agreements and $0.3 million were pledged for certain swap agreements.

The Company has other investments because of interim investment strategies in trust subsidiaries, collateral requirements required in swap and deposit transactions, and Community Reinvestment Act investment requirements. U.S. Treasury bonds in the amount of $505,000 and $517,000 are pledged as collateral in association with the issuance of certain trust preferred securities at December 31, 2007 and December 31, 2006, respectively. These securities had a fair value that approximates their recorded amount for each year presented.

During 2007, the Company sold $538.4 million of available for sale U.S. government sponsored agency and non-agency mortgage-backed securities resulting in a gain of $4.5 million. The Company did not sell any available for sale securities in 2006 or 2005.

The following table summarizes the amortized cost and estimated fair value of securities classified as available for sale (dollars in thousands):

	December 31, 2007	December 31, 2006
Amortized cost	$1,326,656	$615,878
Gross unrealized holding gains	4,647	1,572
Gross unrealized holding losses	(22,695)	—
Estimated fair value	$1,308,608	$617,450

At December 31, 2007 and 2006, no classified available for sale securities had been in a continuous unrealized loss position for greater than twelve months.

The unrealized losses on securities-available for sale amounted to $22.7 million on $843.9 million of AAA rated investments in agency and non-agency collateralized mortgage obligations ("CMOs") at December 31, 2007. These CMOs consist of interests in investment vehicles backed by mortgage loans. In all of the CMOs, the Company's investment is senior to a subordinated tranche(s) which have first loss exposure. Management concluded these unrealized losses are temporary in nature since they are not related to the underlying credit quality of the issuers, and the Company has the intent and ability to hold these investments for a time necessary to recover its cost or will ultimately recover its cost at maturity (i.e. these investments have contractual maturities that, absent credit default, ensure that the Company will ultimately recover its cost). The Company believes that these losses are primarily related to market interest rates and credit spreads and not underlying credit issues associated with the issuers of the obligations. The CMOs were purchased in the fourth quarter of 2006 and first quarter of 2007 and have not experienced any losses to date. The Company does not believe it should have any loss of principal on these investments given its senior position and the protection that the subordinated classes provide. The Company did determine that $2.8 million of the unrealized loss on one of its CMOs was other-than-temporary in nature and as a result recognized a loss on such security. The $2.8 million represented a premium on the security. Although the Company, has the ability and intent to hold the CMO until it recovers to par it does not expect to hold the security beyond that point. As such, the premium was charged to operations in 2007.

As a result of the Company's periodic reviews for impairment in accordance with EITF 99-20, *Recognition of Interest Income and Impairment on Certain Investments* ("EITF 99-20"), during the year ended December 31, 2007, the Company recorded $18.4 million in impairment charges on residual securities available for sale from private-label securitizations completed in 2006 and 2005. The $18.4 million in impairment charges on residual securities available for sale resulted from unfavorable trends in the mortgage industry, benchmarking procedures applied against available industry data, and the Company's own experience that resulted in adjusting the critical assumptions utilized in valuing such securities relating to prepayment speeds, expected credit losses and the discount rate. During 2007, the Company increased its credit loss estimates from 1.25% on its HELOC residual assets to 2.88% for the 2005 securitization and 4.99% for the 2006 securitization. The Company increased the credit loss estimates for its 2006 second mortgage securitization from 1.50% to 2.86%. Further, the Company increased the discount rate assumption from 15% to 20% during 2007 for all available-for-sale residual assets.

The $6.1 million in impairment charges incurred during 2006 on our residual securities available for sale resulted from changes in the interest rate environment, benchmarking procedures applied against updated industry data and third party valuation data that resulted in adjusting the critical prepayment speed assumption utilized in valuing such security. Specifically, the Company completed a private-label securitization of home equity lines of credit in the fourth quarter of 2005. As short-term interest rates increased throughout the fourth quarter of 2005 and the first quarter of 2006 and the yield curve flattened, the prepayment speed of the portfolio increased at a much higher rate than anticipated by management. Management attributed this to fixed rate loans that became available at lower rates than the adjustable-rate HELOC loans in the securitization pool. The Company also noted that this increased prepayment speed with HELOCs was occurring industry wide. The appropriateness of adjusting the model's prepayment speed upward was validated with both a third party valuation firm and with backtesting procedures. Based on this information, the Company adjusted the cash flow model to incorporate the updated prepayment speed during the first quarter of 2006. At March 31, 2006, a significant deterioration of the residual security was determined to have occurred. The Company further analyzed the result and determined that approximately $3.5 million of the deterioration was other than temporary. As the yield curve continued to flatten and even invert during the third and fourth quarters of 2006, prepayment speeds accelerated further. Additionally, based on the Company's analysis it was believed that the inverted yield curve would not be a short term phenomenon. Based on these factors and Company cash flow models, it was determined that additional other than temporary impairment had taken place. Such amounts were recorded as identified and resulted in the $6.1 million in impairment charges for 2006.

The fair value of residual securities is determined by discounting estimated net future cash flows using discount rates that approximate current market rates and expected prepayment rates. Estimated net future cash flows include assumptions related to expected credit losses on these securities. The Company maintains a model that evaluates the default rate and severity of loss on the residual securities' collateral, considering such factors as loss experience, delinquencies, loan-to-value ratio, borrower credit scores and property type.

The fair value of all other non-agency and agency mortgage-backed securities is estimated based on market information.

As of December 31, 2007, the aggregate amount of available for sale securities from each of the following non-agency issuers were greater than 10% of the Company's stockholders' equity.

Name of Issuer	Amortized Cost	Fair Market Value
	(Dollars in thousands)	
Countrywide Alternative Loan Trust	$129,613	$127,192
Countrywide Home Loans	267,239	264,777
Flagstar Home Equity Loan Trust 2006-1	267,397	251,251
Goldman Sachs Mortgage Company	91,575	91,178
JP Morgan Mortgage Trust	88,116	86,847
	$843,940	$821,245

The following table summarizes the amortized cost and estimated fair value of mortgage-backed securities classified as held to maturity (dollars in thousands):

	December 31,	
	2007	2006
Amortized cost	$1,255,431	$1,565,420
Gross unrealized holding gains	33,956	17,382
Gross unrealized holding losses	(304)	(4,420)
Estimated fair value	$1,289,083	$1,578,382

The mortgage-backed securities held to maturity have contractual maturities ranging from 2008 through 2046. Actual maturities will differ from contractual maturities because the underlying mortgages may be prepaid without penalties.

At December 31, 2007 and 2006, no securities classified as held-to-maturity had been in a continuous unrealized loss position for more than a twelve month period.

Note 5 — Loans Available for Sale

The following table summarizes loans available for sale (dollars in thousands):

	December 31, 2007	December 31, 2006
Mortgage loans	$3,083,779	$3,146,943
Consumer loans	170,891	41,050
Second mortgage loans	256,640	802
Total	$3,511,310	$3,188,795

These loans had an aggregate fair value that approximates their recorded amount for each year presented. The majority of the mortgage loans were originated or acquired in the fourth quarter of the respective year.

Note 6 — Loans Held for Investment

Loans held for investment are summarized as follows (dollars in thousands):

	December 31, 2007	December 31, 2006
Mortgage loans	$5,823,952	$6,211,765
Second mortgage loans	56,516	715,154
Commercial real estate loans	1,542,104	1,301,819
Construction loans	90,401	64,528
Warehouse lending	316,719	291,656
Consumer loans	281,746	340,157
Commercial loans	22,959	14,606
Total	8,134,397	8,939,685
Less allowance for loan losses	(104,000)	(45,779)
Total	$8,030,397	$8,893,906

Activity in the allowance for loan losses is summarized as follows (dollars in thousands):

	For the Years Ended December 31, 2007	2006	2005
Balance, beginning of period	$ 45,779	$ 39,140	$ 38,318
Provision charged to operations	88,297	25,450	18,876
Charge-offs	(33,659)	(21,613)	(19,907)
Recoveries	3,583	2,802	1,853
Balance, end of period	$104,000	$ 45,779	$ 39,140

Loans on which interest accruals have been discontinued totaled approximately $197.1 million at December 31, 2007 and $57.1 million at December 31, 2006. Interest on these loans is recognized as income when collected. Interest that would have been accrued on such loans totaled approximately $6.8 million, $3.8 million, and $4.1 million during 2007, 2006, and 2005, respectively. There are no loans greater than 90 days past due still accruing interest at December 31, 2007 and 2006.

A loan is impaired when it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement.

Impaired loans are as follows (dollars in thousands):

	December 31,		
	2007	2006	2005
Impaired loans with no allowance for loan losses allocated	$ 22,307	$15,228	$27,876
Impaired loans with allowance for loan losses allocated	112,044	10,934	6,556
Total impaired loans	$134,351	$26,162	$34,432
Amount of the allowance allocated to impaired loans	$ 34,937	$ 1,119	$ 1,618
Average investment in impaired loans	$ 70,582	$28,469	$27,048
Cash-basis interest income recognized during impairment	$ 2,324	$ 1,792	$ 2,099

Those impaired loans not requiring an allowance represent loans for which the fair value of the collateral less estimated selling costs exceeded the recorded investments in such loans. At December 31, 2007, approximately 82% of the total impaired loans were evaluated based on the fair value of related collateral.

Note 7 — Private-label Securitization Activity

On March 15, 2007, the Company sold $620.9 million in closed-ended, fixed and adjustable rate second mortgage loans (the "2007 Second Mortgage Securitization") and recorded $22.6 million in residual interests and servicing assets as a result of the non-agency securitization. On June 30, 2007, the Company completed a secondary closing for $98.2 million and recorded an additional $4.2 million in residual interests. The residual interests are categorized as securities classified as trading and are, therefore, recorded at fair value. Any gains or losses realized on the sale of such securities and any subsequent changes in unrealized gains and losses are reported in the consolidated statement of operations.

Key economic assumptions used in determining the fair value of residual interests at the time of the securitization are as follows:

	Prepayment Speed	Projected Credit Losses	Annual Discount Rate	Weighted-Average Life (in years)
2007 Second Mortgage Securitization	26%	1.50%	15.0%	3.8

The Company recorded $11.2 million in residual interests as of December 31, 2006, as a result of its non-agency securitization of $302 million in home equity line of credit loans (the "2006 HELOC Securitization"). In addition, through November 2007, draws on the home equity lines of credit in the trust established in the 2006 HELOC Securitization were purchased from the Company by the trust, resulting in additional residual interests to the Company. These residual interests were recorded as securities available for sale and are therefore, recorded at fair value. Any gains or losses realized on the sale of such securities or any unrealized losses that were deemed to be other-than-temporarily impaired ("OTTI") were reported in the consolidated statement of operations. All unrealized gains or losses that were deemed to be temporary were reported in the consolidated statement of stockholders' equity and comprehensive income under accumulated other comprehensive income.

In accordance with the terms of the securitization, credit losses in the 2006 HELOC Securitization exceeded losses as originally modeled. As such, the monoline insurer that protects the bondholders determined that the status of the securitization should be changed to "rapid amortization." During the rapid amortization period, the Company will no longer be reimbursed for draws on the home equity lines of credit until after the bondholders are paid off. Therefore, this status has the effect of extending the time period for which the Company's advances are outstanding and may result in the Company not receiving reimbursement for all of the funds advanced. As of December 31, 2007, the Company advanced $4.3 million of funds under this arrangement and does not believe that a liability has been incurred under this arrangement.

On April 28, 2006, the Company completed a guaranteed mortgage securitization transaction of approximately $400.0 million of fixed second mortgage loans that the Company held at the time in its investment portfolio. The transaction was treated as a recharacterization of loans held for investment to mortgage-backed securities held to maturity and, therefore, no gain on sale was recorded. The securitization resulted in the Company recording a residual interest of approximately $9.9 million that is carried as a security available for sale.

The Company recorded $26.1 million in residual interests as of December 31, 2005, as a result of its non-agency securitization of $600 million in home equity line of credit loans (the "2005 HELOC Securitization"). In addition, each month draws on the home equity lines of credit in the trust established in the 2005 HELOC Securitization are purchased from the Company by the trust, resulting in additional residual interests to the Company. These residual interests are recorded as securities available for sale and are, therefore, recorded at fair value. Any gains or losses realized on the sale of such securities or any unrealized losses that are deemed to be other-than-temporarily impaired ("OTTI") are reported in the consolidated statement of operations. All unrealized gains or losses that are deemed to be temporary are reported in the consolidated statement of stockholders' equity and comprehensive income under accumulated other comprehensive income.

At December 31 2007, key assumptions used in determining the value of residual interests resulting from the securitizations were as follows:

	Prepayment Speed	Projected Credit Losses	Annual Discount Rate	Weighted-Average Life (in years)
2005 HELOC Securitization	28.0%	2.88%	20.0%	3.5
2006 HELOC Securitization	28.0%	4.99%	20.0%	4.3
2006 Second Mortgage Securitization	16.0%	2.86%	20.0%	4.5
2007 Second Mortgage Securitization	18.0%	3.28%	20.0%	5.6

Certain cash flows received from the securitization trusts were as follows (dollars in thousands):

	For the Years Ended December 31,	
	2007	2006
Proceeds from new securitizations	$664,927	$302,182
Proceeds from collections reinvested in securitizations	166,361	73,122
Servicing fees received	6,884	2,259
Loan repurchases for representations and warranties	(642)	(752)

The tables below set forth key economic assumptions and the hypothetical sensitivity of the fair value of residual interests to an immediate adverse change in any single key assumption. Changes in fair value based on 10% and 20% variations in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. The effect of a variation in a particular assumption on the fair value of the residual interest is calculated without changing any other assumptions. In practice, changes in one factor may result in changes in other factors, such as increases in market interest rates that may magnify or counteract sensitivities. The dollar impacts on the residual and servicing asset in the table below represents decreases to the value of the respective assets.

	Fair Value	Prepayment Speed	Projected Credit Losses	Discount Rate
	(Dollars in thousands)			
HELOC Securitizations				
Residual securities as of December 31, 2007	$30,180	28.0%	3.68%	20.0%
Impact on fair value of 10% adverse change in assumption		$1,856	$ 853	$1,493
Impact on fair value of 20% adverse change in assumption		$3,568	$2,255	$2,857
Servicing asset as of December 31, 2007	$ 2,881			
Impact on fair value of 10% adverse change of assumptions		$ 319	$ 1	$ 31
Impact on fair value of 20% adverse change of assumptions		$ 600	$ 3	$ 61
Second Mortgage Securitizations				
Residual securities as of December 31, 2007	$16,856	17.6%	3.20%	20.0%
Impact on fair value of 10% adverse change in assumption		$ 997	$2,184	$1,850
Impact on fair value of 20% adverse change in assumption		$1,897	$3,394	$3,194
Servicing asset as of December 31, 2007	$ 8,980			
Impact on fair value of 10% adverse change of assumptions		$ 629	$ 13	$ 147
Impact on fair value of 20% adverse change of assumptions		$1,193	$ 26	$ 290

Credit Risk on Securitization

With respect to the issuance of private-label securitizations, the Company retains certain limited credit exposure in that it retains non-investment grade residual securities in addition to customary representations and warranties. The Company does not have credit exposure associated with non-performing loans in securitizations beyond its investment in retained interests in non-investment grade residuals and draws on HELOCS that it funds and which are not reimbursed by the respective trust. The value of the Company's retained interests reflects the Company's credit loss assumptions as to the underlying collateral pool. To the extent that actual credit losses exceed the assumptions, the value of the Company's non-investment grade residual securities and unreimbursed draws will be diminished.

The following table summarizes the collateral balance associated with the Company's servicing portfolio of sold loans and the balance of related non-investment grade residual securities retained at December 31, 2007 (dollars in thousands):

	Total Loans Serviced	Balance of Retained Assets with Credit Exposure Residuals
Private-label securitizations	$ 1,405,010	$47,036
Government sponsored agencies	31,081,476	—
Other investors	851	—
Total	$32,487,337	$47,036

Mortgage loans that have been securitized in private-label securitizations at December 31, 2007 and 2006 that are sixty days or more past due and the credit losses incurred in the securitization trusts are presented below (dollars in thousands):

	Total Principal Amount of Loans Outstanding		Principal Amount of Loans 60 Days or More Past Due		Credit Losses (Net of Recoveries)	
	December 31,		December 31,		For the Years Ended December 31,	
	2007	2006	2007	2006	2007	2006
Securitized mortgage loans	$1,405,010	$968,423	$19,783	$2,682	$29,303	$3,938

Note 8 — FHLB Stock

The Company's investment in FHLB stock totaled $348.9 million and $277.6 million at December 31, 2007 and 2006, respectively. As a member of the FHLB, the Company is required to hold shares of FHLB stock in an amount at least equal to 1.0% of the aggregate unpaid principal balance of its mortgage loans, home purchase contracts and similar obligations at the beginning of each year or 1/20th of its FHLB advances, whichever is greater. Dividends received on the stock equaled $14.4 million, $13.7 million, and $10.7 million for the years ended December 31, 2007, 2006 and 2005, respectively. These dividends were recorded in the consolidated statement of operations as other fees and charges.

Note 9 — Repossessed Assets

Repossessed assets include the following (dollars in thousands):

	December 31,	
	2007	2006
One-to-four family properties	$101,936	$74,548
Commercial properties	7,338	6,447
Repossessed assets	$109,274	$80,995

Note 10 — Premises and Equipment

Premises and equipment balances are as follows (dollars in thousands):

	December 31,	
	2007	2006
Land	$ 82,413	$ 70,437
Office buildings	143,370	135,186
Computer hardware and software	93,551	130,574
Furniture, fixtures and equipment	82,157	72,173
Automobiles	283	285
Total	401,774	408,655
Less accumulated depreciation	(164,122)	(189,412)
	$ 237,652	$ 219,243

Depreciation expense amounted to approximately $20.5 million, $26.9 million, and $30.7 million, for the years ended December 31, 2007, 2006 and 2005, respectively.

The Company conducts a portion of its business from leased facilities. Such leases are considered to be operating leases based on their lease terms. Lease rental expense totaled approximately $9.4 million, $8.7 million, and $9.8 million for the years ended December 31, 2007, 2006 and 2005, respectively.

The following outlines the Company's minimum contractual lease obligations as of December 31, 2007 (dollars in thousands):

2008	$ 6,335
2009	4,739
2010	3,516
2011	1,968
2012	1,116
Thereafter	1,635
Total	$19,309

Note 11 — Mortgage Servicing Rights

Included in Non-Interest Income under the caption Loan Administration are contractually specified servicing fees, late fees and ancillary fees amounting to $91.1 million, $82.6 million and $103.3 million for the years ended December 31, 2007, 2006 and 2005, respectively.

Mortgage loans serviced for others are not included in the accompanying consolidated financial statements. The unpaid principal balances of these loans are summarized as follows (dollars in thousands):

	December 31,	
	2007	2006
Mortgage loans serviced for:		
FHLMC and FNMA	$28,132,766	$12,566,869
FHLBI	245,437	272,273
GNMA	2,703,273	1,224,010
Flagstar Trusts	1,405,010	968,423
Other investors	851	928
Total	$32,487,337	$15,032,503

Not included in the above totals are $0.5 million and $229.4 million of mortgage loans at December 31, 2007 and December 31, 2006, respectively, that are being serviced on a temporary basis in connection with the sale of mortgage servicing rights.

Mortgage loans serviced for others were geographically disbursed throughout the United States. As of December 31, 2007, approximately 12.8% of these properties are located in Michigan (measured by principal balance), and another 40.0% were located in the states of Florida (10.4%), California (9.0%), Texas (8.7%) Washington (5.6%), Maryland (3.3%) and Colorado (3.0%). No other state contains more than 4% of the properties collateralizing these serviced loans.

Custodial accounts maintained in connection with the above mortgage servicing rights (including the above mentioned subservicing) were approximately $422.5 million and $237.0 million at December 31, 2007 and 2006 respectively. These amounts include payments for principal, interest, taxes, and insurance collected on behalf of the individual investor.

The following is an analysis of the changes in the recorded value of the Company's mortgage servicing rights (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
Balance, beginning of period	$173,288	$ 315,678	$ 187,975
Capitalization	346,348	223,934	328,954
Sales	(27,734)	(296,163)	(106,703)
Amortization	(78,344)	(69,562)	(94,548)
Valuation allowance	428	(599)	—
Balance, end of period	$413,986	$ 173,288	$ 315,678

Throughout 2007, the fair value of the MSRs capitalized was based upon the following weighted-average assumptions: (1) a discount rate of 9.6%; (2) an anticipated loan prepayment rate of 17.1% (i.e. CPR); (3) a weighted-average life of 6.1 years; and (4) servicing costs per conventional loan of $42 and $45 for each government or adjustable-rate loan, respectively. Throughout 2006, the fair value of the MSRs capitalized was based on the following weighted-average assumptions; (1) a discount rate of 9.8%; (2) an anticipated loan prepayment rate of 28.5% (i.e. CPR); (3) a weighted-average life of 5.8 years; and (4) servicing costs per convention loan of $40 and $52 for each government or adjustable rate loan, respectively.

Changes in the valuation allowance for impairment of MSRs are as follows (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
Balance, beginning of period	$ 599	$ —	$—
Provision for valuation	(428)	599	—
Permanent impairment	—	—	—
Balance, end of period	$ 171	$599	$—

At December 31, 2007 and 2006, the estimated fair value of the mortgage loan-servicing portfolio was $457.9 million and $197.6 million, respectively. At December 31, 2007, the fair value of each MSR was based upon the following weighted-average assumptions: (1) a discount rate of 9.2%; (2) an anticipated loan prepayment rate of 16.3% (i.e. CPR); (3) a weighted-average life of 5.4 years and (4) servicing costs per conventional loan of $42 and $45 for each government or adjustable-rate loan, respectively.

Note 12 — Deposit Accounts

The deposit accounts are as follows (dollars in thousands):

	December 31, 2007	December 31, 2006
Demand accounts	$ 436,239	$ 380,162
Savings accounts	237,762	144,460
Money market demand accounts	531,587	608,282
Certificates of deposit	3,870,828	3,763,781
Total retail deposits	5,076,416	4,896,685
Municipal deposits	1,545,395	1,419,964
National accounts	1,141,549	1,062,646
Company controlled deposits	473,384	244,193
Total deposits	$8,236,744	$7,623,488

At December 31, 2007, municipal deposits included $1.5 billion of certificates of deposit with maturities typically less than one year and $72.0 million in checking and savings accounts. At December 31, 2006, municipal deposits included $1.3 billion of certificates of deposit and $87.3 million in checking and savings accounts.

Non-interest-bearing deposits included in the demand accounts and money market demand accounts balances at December 31, 2007 and 2006, were approximately $0.6 billion and $0.9 billion, respectively.

The aggregate amount of certificates of deposit with a minimum denomination of $100,000 was approximately $2.8 billion and $2.6 billion at December 31, 2007 and 2006, respectively. The following table indicates the scheduled maturities for certificates of deposit with a minimum denomination of $100,000 (dollars in thousands):

	December 31, 2007	December 31, 2006
Three months or less	$1,250,017	$1,268,286
Over three months to six months	820,475	601,625
Over six months to twelve months	539,156	429,199
One to two years	111,190	179,393
Thereafter	79,084	120,305
Total	$2,799,922	$2,598,808

The following table indicates the scheduled maturities of the Company's certificates of deposit with a minimum denomination of $100,000 by acquisition channel as of December 31, 2007 (dollars in thousands):

	Consumer Direct	Municipal	National Accounts	Total
Twelve months or less	$1,213,468	$1,394,611	$1,569	$2,609,648
One to two years	105,403	5,787	—	111,190
Two to three years	35,087	205	—	35,292
Three to four years	19,917	—	—	19,917
Four to five years	19,836	—	—	19,836
Thereafter	4,039	—	—	4,039
Total	$1,397,750	$1,400,603	$1,569	$2,799,922

Note 13 — FHLB Advances

The portfolio of FHLB advances includes floating rate daily adjustable advances, fixed rate putable advances and fixed rate term advances. The following is a breakdown of the advances outstanding (dollars in thousands):

	December 31,			
	2007		2006	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate
Fixed rate putable advances	$1,900,000	4.13%	$ 500,000	4.24%
Short-term fixed rate term advances	1,851,000	4.07%	2,757,000	4.95%
Long-term fixed rate term advances	2,550,000	4.69%	2,150,000	4.28%
Total	$6,301,000	4.34%	$5,407,000	4.62%

The portfolio of putable FHLB advances held by the Company matures in 2012 and may be called by the FHLB based on FHLB volatility models. During 2008 and thereafter, the FHLB may call $1.6 billion of the putable advances. During 2009 and thereafter, the FHLB may call the remaining $0.3 billion of putable advances.

The following indicates certain information related to the FHLB advances (dollars in thousands):

	For The Years Ended December 31,		
	2007	2006	2005
Maximum outstanding at any month end	$6,392,000	$5,407,000	$5,373,279
Average balance	5,847,888	4,270,660	4,742,079
Average interest rate	4.64%	4.40%	3.85%

The following outlines the Company's FHLB advance final maturity dates as of December 31, 2007 (dollars in millions):

2008	$1,851
2009	650
2010	650
2011	500
2012	2,150
Thereafter	500
Total	$6,301

The Company has the authority and approval from the FHLB to utilize a total of $7.5 billion in collateralized borrowings. Pursuant to collateral agreements with the FHLB, advances are collateralized by non-delinquent single-family residential mortgage loans.

Note 14 — Security Repurchase Agreements

The following table presents security repurchase agreements outstanding (dollars in thousands):

	December 31,			
	2007		2006	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate
Security repurchase agreements	$108,000	4.27%	$990,806	5.31%

These repurchase agreements have maturities of less than 36 months. At December 31, 2007 and 2006, security repurchase agreements were collateralized by $107.3 million and $1.0 billion of mortgage-backed securities held to maturity, respectively.

The following table indicates certain information related to the security repurchase agreements (dollars in thousands):

	For The Years Ended December 31,		
	2007	2006	2005
Maximum outstanding at any month end	$1,793,026	$1,259,812	$1,101,242
Average balance	954,772	1,028,916	187,585
Average interest rate	5.39%	5.09%	4.24%

Note 15 — Long Term Debt

The following table presents long-term debt (dollars in thousands):

	December 31, 2007	December 31, 2006
Junior subordinated notes related to trust preferred securities		
Floating 3 month LIBOR plus 3.25%(1) (8.11% and 8.62% at December 31, 2007 and 2006, respectively), matures 2032	$ 25,774	$ 25,774
Fixed 6.55%(2), matures 2033	25,774	25,774
Fixed 6.75%(2), matures 2033	25,780	25,780
Floating 3 month LIBOR plus 2.00% (7.24% and 7.37% at December 31, 2007 and 2006, respectively), matures 2035	25,774	25,774
Floating 3 month LIBOR plus 2.00% (7.24% and 7.37% at December 31, 2007 and 2006, respectively), matures 2035	25,774	25,774
Fixed 6.47%(3), matures 2035	51,547	51,547
Floating 3 month LIBOR plus 1.50%(4) (6.74% and 6.87% at December 31, 2007 and 2006, respectively), matures 2035	25,774	25,774
Floating 3 month LIBOR plus 1.45% (6.44% at December 31, 2007, matures 2037)	25,774	—
Floating 3 month LIBOR plus 2.50% (7.49% at December 31, 2007, matures 2037)	15,464	—
Subtotal	247,435	206,197
Other Debt		
Fixed 7.00% due 2013	1,250	1,275
Total long-term debt	$248,685	$207,472

(1) As part of the transaction, the Company entered into an interest rate swap with the placement agent under which the Company is required to pay 6.88% fixed rate on a notional amount of $25 million and will receive a floating rate equal to three month LIBOR plus 3.25%. The swap matured on December 26, 2007. The securities are callable by the Company after December 26, 2007.

(2) In 2008, the callable date, the rate converts to a variable rate equal to three month LIBOR plus 3.25%, adjustable quarterly. The securities are callable by the Company after February 26, 2008 and March 26, 2008.

(3) In 2010, the callable date, the rate converts to a variable rate equal to three month LIBOR plus 2.00% adjustable quarterly. The securities are callable by the Company after March 31, 2010.

(4) As part of the transaction, the Company entered into an interest rate swap with the placement agent, under which the Company is required to pay 4.33% fixed rate on a notional amount of $25 million and will receive a floating rate equal to three month LIBOR. The swap matures on October 7, 2010. The securities are callable by the Company after October 7, 2010.

Interest on all junior subordinated notes related to trust preferred securities is payable quarterly. Under these arrangements, the Company has the right to defer dividend payments to the trust preferred security holders for up to five years.

The following presents the aggregate annual maturities of long term-debt obligations (based on final maturity dates) as of December 31, 2007 (dollars in thousands):

2008	$ 25
2009	25
2010	25
2011	25
2012	25
Thereafter	248,560
Total	$248,685

Note 16 — Federal Income Taxes

Total federal income tax provision (benefit) is allocated as follows (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
(Loss) earnings from operations	$(19,589)	$40,819	$44,090
Stockholders' equity, for the tax (benefit) expense from stock-based compensation	25	(1,000)	(8,379)
Stockholders' equity, for the tax effect of other comprehensive income (loss)	(8,979)	(1,222)	1,341
	$(28,543)	$38,597	$37,052

Components of the (benefit) provision for federal income taxes from operations consist of the following (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
Current provision (benefit)	$(58,308)	$ 93,634	$(12,342)
Deferred provision (benefit)	38,719	(52,815)	56,432
	$(19,589)	$ 40,819	$ 44,090

The Company's effective tax rate differs from the statutory federal tax rate. The following is a summary of such differences (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
(Benefit) provision at statutory federal income tax rate (35)%	$(20,585)	$40,607	$43,384
Increase resulting from other, net	996	212	706
(Benefit) provision at effective federal income tax rate	$(19,589)	$40,819	$44,090

The details of the net tax liability are as follows (dollars in thousands):

	December 31,	
	2007	2006
Deferred tax assets:		
Allowance for loan and other losses	$ 42,032	$ 32,891
Loan securitizations	8,306	723
Premises and equipment	4,316	3,509
Non-accrual interest revenue	2,554	1,068
Mark-to-market adjustments	2,135	—
Accrued vacation pay	1,892	1,605
Other	2,857	995
	64,092	40,791
Deferred tax liabilities:		
Mortgage loan servicing rights	(111,187)	(59,491)
Federal Home Loan Bank stock dividends	(8,007)	(8,543)
State income taxes	(4,396)	(2,545)
Deferred loan costs and fees	—	(4,837)
Mark-to-market adjustments	—	(4,400)
Unrealized hedging gains	(132)	(2,258)
Other	(120)	(224)
	(123,842)	(82,298)
Net deferred tax liability	(59,750)	(41,507)
Current federal income taxes receivable	59,778	11,833
Income taxes receivable (payable)	$ 28	$(29,674)

The Company has not provided deferred income taxes for the Bank's pre-1988 tax bad debt reserves of approximately $4 million because it is not anticipated that this temporary difference will reverse in the foreseeable future. Such reserves would only be taken into taxable income if the Bank, or a successor institution, liquidates, redeems shares, pays dividends in excess of earnings and profits, or ceases to qualify as a bank for tax purposes.

In 2006, the FASB issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes — an Interpretation of FASB Statement 109*, ("FIN 48") to clarify the accounting treatment for uncertain income tax positions when applying FASB Statement 109. Effective January 1, 2007, the Company adopted FIN 48. As a result, the Company recorded the estimated value of its uncertain tax positions by increasing its tax liability by $1.4 million and recording a corresponding reduction to retained earnings.

The Company's income tax returns are subject to review and examination by federal, state and local government authorities. On an ongoing basis, numerous federal, state and local examinations are in progress and cover multiple tax years. As of December 31, 2007, the Internal Revenue Service had completed its examination of the Company through the taxable year ended December 31, 2003. The years open to examination by state and local government authorities vary by jurisdiction.

The following table provides a reconciliation of the total amounts of unrecognized tax benefits for the year ended December 31, 2007 (dollars in thousands):

Unrecognized tax benefits at adoption, opening balance	$4,725
Gross increases — tax positions in prior periods	676
Gross decreases — tax positions in prior periods	(64)
Gross increases — current period tax positions	—
Settlements	767
Lapse of statute of limitations	—
Unrecognized tax benefits, ending balance	$6,104

Included in the balance at December 31, 2007, are $4.7 million of tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. Because of the impact of deferred tax accounting, other than interest and penalties, the disallowance of a shorter deductibility period does not affect the annual effective tax rate but would accelerate the payment of cash to the taxing authority to an earlier period.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense and/or franchise tax expense. For the year ended December 31, 2007, the Company recognized interest expense or approximately $450,000 and no penalty costs in its statement of operations and statement of financial condition, respectively.

Approximately $5.5 million of the above tax positions are expected to reverse during the next 12 months.

Note 17 — Secondary Market Reserve

The following table shows the activity in the secondary market reserve (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
Balance, beginning of period,	$ 24,200	$ 17,550	$ 19,002
Provision			
Charged to gain on sale for current loan sales	9,899	5,897	5,328
Charged to other fees and charges for changes in estimates	3,699	14,312	7,156
Total	13,598	20,209	12,484
Charge-offs, net	(10,198)	(13,559)	(13,936)
Balance, end of period	$ 27,600	$ 24,200	$ 17,550

Reserve levels are a function of expected losses based on actual pending and expected claims and repurchase requests, historical experience and loan volume. While the ultimate amount of repurchases and claims is uncertain, management believes that reserves are adequate. We will continue to evaluate the adequacy of our reserves and may continue to allocate a portion of our gain on sale proceeds to these reserves going forward.

Note 18 — Employee Benefit Plans

The Company maintains a 401(k) plan for its employees. Under the plan, eligible employees may contribute up to 60% of their annual compensation, subject to a maximum amount proscribed by law. The maximum annual contribution was $15,500 for 2007, $15,000 for 2006 and $14,000 for 2005. Participants who were 50 years old or older prior to the end of the year could make additional "catch-up" contributions of up to $5,000, $5,000, and $4,000 for 2007, 2006, and 2005, respectively. The Company currently provides a matching contribution up to 3% of an employee's annual compensation up to a maximum of $6,750. The Company's contributions vest at a rate such that an employee is fully vested after five years of service. The Company's contributions to the plan for the years ended December 31, 2007, 2006, and 2005 were approximately $3.3 million, $3.1 million, and $3.3 million, respectively. The Company may also make discretionary contributions to the plan; however, none have been made.

Prior to March 31, 2005, the Company offered a deferred compensation plan to employees. The deferred compensation plan allowed employees to defer up to 25% of their annual compensation and directors to defer all of their compensation. Funds deferred remained the property of the Company. The Company discontinued this compensation plan March 31, 2005.

Note 19 — Contingencies and Commitments

The Company is involved in certain lawsuits incidental to its operations. Management, after review with its legal counsel, is of the opinion that resolution of such litigation will not have a material effect on the Company's financial condition, results of operations, or liquidity.

A substantial part of the Company's business has involved the origination, purchase, and sale of mortgage loans. During the past several years, numerous individual claims and purported consumer class action claims were commenced against a number of financial institutions, their subsidiaries and other mortgage lending institutions generally seeking civil statutory and actual damages and rescission under the federal Truth in Lending Act, as well as remedies for alleged violations of various state and federal laws, restitution or unjust enrichment in connection with certain mortgage loan transactions.

The Company has a substantial mortgage loan-servicing portfolio and maintains escrow accounts in connection with this servicing. During the past several years, numerous individual claims and purported consumer class action claims were commenced against a number of financial institutions, their subsidiaries and other mortgage lending institutions generally seeking declaratory relief that certain of the lenders' escrow account servicing practices violate the Real Estate Settlement Practices Act and breach the lenders' contracts with borrowers. Such claims also generally seek actual damages and attorney's fees.

In addition to the foregoing, mortgage lending institutions have been subjected to an increasing number of other types of individual claims and purported consumer class action claims that relate to various aspects of the origination, pricing, closing, servicing, and collection of mortgage loans that allege inadequate disclosure, breach of contract, or violation of state laws. Claims have involved, among other things, interest rates and fees charged in connection with loans, interest rate adjustments on adjustable rate loans, timely release of liens upon payoffs, the disclosure and imposition of various fees and charges, and the placing of collateral protection insurance.

While the Company has had various claims similar to those discussed above asserted against it, management does not expect that the ultimate resolution of these claims will have a material adverse effect on the Company's financial condition, results of operations, or liquidity.

A summary of the contractual amount of significant commitments is as follows (dollars in thousands):

	December 31,	
	2007	2006
Commitments to extend credit:		
Mortgage loans	$3,141,000	$1,779,000
Commercial	102,000	134,000
Other	3,000	30,000
HELOC trust commitments	167,000	193,000
Standby and commercial letters of credit	112,000	114,000

Commitments to extend credit are agreements to lend. Since many of these commitments expire without being drawn upon, the total commitment amounts do not necessarily represent future cash flow requirements. Certain lending commitments for commercial and mortgage loans to be sold in the secondary market are considered derivative instruments in accordance with SFAS 133. Changes to the fair value of these commitments as a result of changes in interest rates are recorded on the statement of financial condition as either an other asset or other liability. The commitments related to mortgage loans and commercial real estate loans are included in mortgage loans and commercial loans in the above table.

The Company enters into forward contracts for the future delivery or purchase of agency and loan sale contracts. These contracts are considered to be derivative instruments under SFAS 133. Further discussion on derivative instruments is included in Note 24.

The Company had unfunded commitments under its contractual arrangement with the HELOC Securitization trusts to fund future advances on the underlying home equity lines of credit.

Standby and commercial letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. Standby letters of credit generally are contingent upon the failure of the customer to perform according to the terms of the underlying contract with the third party, while commercial letters of credit are issued specifically to facilitate commerce and typically results in the commitment being drawn on when the underlying transaction is consummated between the customer and the third party.

The credit risk associated with loan commitments, standby and commercial letters of credit is essentially the same as that involved in extending loans to customers and is subject to normal credit policies. Collateral may be obtained based on management's credit assessment of the customer. The guarantee liability for standby and commercial letters of credit was $2.0 million as of December 31, 2007. The Company had no guarantee liability recorded as of December 31, 2006 as estimated credit risk was insignificant.

Note 20 — Regulatory Capital Requirements

The Bank is subject to various regulatory capital requirements administered by the federal 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 consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by regulators about components, risk weightings, and other factors.

Quantitative measures that have been established by regulation to ensure capital adequacy require the Bank to maintain minimum capital amounts and ratios (set forth in the table below). The Bank's primary regulatory agency, the OTS, requires that the Bank maintain minimum ratios of tangible capital (as defined in the regulations) of 1.5%, core capital (as defined) of 3.0%, and total risk-based capital (as defined) of 8.0%. The Bank is also subject to prompt corrective action capital requirement regulations set forth by the FDIC. The FDIC requires the Bank to maintain a minimum of Tier 1 total and core capital (as defined) to risk-weighted assets (as defined), and of core capital (as defined) to adjusted tangible assets (as defined). Management believes, as of December 31, 2007, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2007 and 2006, the most recent guidelines from the OTS categorized the Bank as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," the Bank must maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table below. There are no conditions or events since that notification that management believes have changed the Bank's category.

	Actual		For Capital Adequacy Purposes		Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
As of December 31, 2007						
Tangible capital (to tangible assets)	$ 912,040	5.8%	$236,524	1.5%	N/A	N/A
Core capital (to adjusted tangible assets)	912,040	5.8%	473,048	3.0%	$788,413	5.0%
Tier I capital (to risk weighted assets)	883,516	9.9%	N/A	N/A	536,166	6.0%
Total capital (to risk weighted assets)	952,254	10.7%	714,881	8.0%	893,602	10.0%
As of December 31, 2006						
Tangible capital (to tangible assets)	$ 984,981	6.4%	$231,901	1.5%	N/A	N/A
Core capital (to adjusted tangible assets)	984,981	6.4%	463,802	3.0%	$773,005	5.0%
Tier I capital (to risk weighted assets)	957,388	11.0%	N/A	N/A	520,502	6.0%
Total capital (to risk weighted assets)	1,001,937	11.6%	693,996	8.0%	867,494	10.0%

Note 21 — Accumulated Other Comprehensive (Loss) Income

The following table sets forth the ending balance in accumulated other comprehensive (loss) income for each component (dollars in thousands):

	December 31,		
	2007	2006	2005
Net gain on interest rate swap extinguishment	$ —	$ 101	$1,268
Net unrealized gain on derivatives used in cash-flow hedges	236	4,193	6,068
Net unrealized (loss) gain on securities available for sale	(11,731)	888	498
Ending balance	$(11,495)	$5,182	$7,834

The following table sets forth the changes to other comprehensive (loss) income and the related tax effect for each component (dollars in thousands):

	For the Years Ended December 31,		
	2007	2006	2005
Gain (reclassified to earnings) on interest rate swap extinguishment	$ (155)	$(1,795)	$(2,054)
Related tax benefit	54	628	719
Unrealized gain (loss) on derivatives used in cash-flow hedging relationships	(11,377)	(8,487)	5,804
Related tax (expense) benefit	3,981	2,970	(2,032)
Reclassification adjustment for (gains) losses included in earnings relating to cash flow hedging relationships	5,290	5,603	(685)
Related tax (expense) benefit	(1,851)	(1,960)	240
Unrealized (loss) gain on securities available for sale	(19,414)	805	767
Related tax benefit (expense)	6,795	(416)	(268)
Change	$(16,677)	$(2,652)	$ 2,491

Note 22 — Concentrations of Credit

Properties collateralizing mortgage loans held for investment were geographically disbursed throughout the United States (measured by principal balance and expressed as a percent of the total).

State	December 31, 2007	December 31, 2006
Michigan	10.8%	13.1%
California	26.9	23.1
Florida	13.6	12.6
Washington	4.9	5.0
Colorado	3.8	4.5
Texas	3.4	4.1
Arizona	3.9	3.0
All other states(1)	32.7	34.6
	100.0%	100.0%

(1) — No other state contains more than 3.0% of the total.

A substantial portion of the Company's commercial real estate loan portfolio at December 31, 2007, 63.1%, is collateralized by properties located in Michigan. At December 31, 2006, the Company's commercial real estate portfolio in Michigan was 76.9% of the total portfolio.

Additionally, the following loan products' contractual terms may give rise to a concentration of credit risk and increase the Company's exposure to risk of nonpayment or realization:

(a) Hybrid or ARM loans that are subject to future payment increases

(b) Option power ARM loans that permit negative amortization

(c) Loans under a. or b. above with loan-to-value ratios above 80%

The following table details the unpaid principal balance of these loans at December 31, 2007:

	Held for Investment Portfolio Loans
	(Dollars in thousands)
Amortizing hybrid ARMs	
3/1 ARM	$ 432,812
5/1 ARM	1,152,636
7/1 ARM	107,309
Interest only hybrid ARMs	
3/1 ARM	558,403
5/1 ARM	1,930,657
7/1 ARM	187,521
Option power ARMs	82,754
All other ARMs	306,487
	$4,758,579

Of the loans listed above, the following have original loan-to-value ratios exceeding 80%.

	Principal Outstanding At December 31, 2007
	(Dollars in thousands)
Loans with original loan-to-value ratios above 80%	
> 80%< = 90%	$342,317
> 90%< = 100%	235,611
>100%	536
	$578,464

Note 23 — Related Party Transactions

The Company has and expects to have in the future, transactions with certain of the Company's directors and principal officers. Such transactions were made in the ordinary course of business and included extensions of credit and professional services. With respect to the extensions of credit, all were made on substantially the same terms, including interest rates and collateral, as those prevailing at the same time for comparable transactions with other customers and did not, in management's opinion, involve more than normal risk of collectibility or present other unfavorable features. At December 31, 2007, the balance of the loans attributable to directors and principal officers totaled $4.1 million, with the unused lines of credit totaling $7.0 million. At December 31, 2006, the balance of the loans attributable to directors and principal officers totaled $6.9 million, with the unused lines of credit totaling $11.5 million. During 2007 and 2006, the Company purchased $102.7 million and $96.1 million in mortgage loans from correspondents and brokers affiliated with directors and executive officers, during the ordinary course of business.

Note 24 — Derivative Financial Instruments

The Company follows the provisions of SFAS 133, as amended, for its derivative instruments and hedging activities, which require it to recognize all derivative instruments on the consolidated statements of financial condition at fair value. The following derivative financial instruments were identified and recorded at fair value as of December 31, 2007 and 2006:

FNMA, FHLMC and other forward contracts
Rate lock commitments
Interest rate swap agreements

Generally speaking, if interest rates increase, the value of the Company's rate lock commitments and funded loans decrease and loan sale margins are adversely impacted. The Company hedges the risk of overall changes in fair value of loans held for sale and rate lock commitments generally by selling forward contracts on securities of Fannie Mae, Freddie Mac and Ginnie Mae. Under SFAS 133, certain of these positions may qualify as a fair value hedge of a portion of the funded loan portfolio and result in adjustments to the carrying value of designated loans through gain on sale based on value changes attributable to the hedged risk. The forward contracts used to economically hedge the loan commitments are accounted for as non-designated hedges and naturally offset rate lock commitment mark-to-market gains and losses recognized as a component of gain on loan sale. The Bank recognized pre-tax gains of $4.4 million and $4.5 million for the years ended December 31, 2007 and 2006, respectively, and pre-tax losses of $2.9 million for the year ended December 31, 2005, on its hedging activity.

The Company uses interest rate swap agreements to reduce its exposure to interest rate risk inherent in a portion of the current and anticipated borrowings and advances. A swap agreement is a contract between two parties to exchange cash flows based on specified underlying notional amounts and indices. Under SFAS 133, the swap agreements used to hedge the Company's anticipated borrowings and advances qualify as cash flow hedges. Derivative gains and losses reclassed from accumulated other comprehensive (loss) income to current period operations are included in the line item in which the hedge cash flows are recorded. At December 31, 2007 and 2006, accumulated other comprehensive (loss) income included a deferred after-tax net gain of $0.2 million and $4.2 million, respectively, related to derivatives used to hedge funding cash flows. See Note 21 for further detail of the amounts included in accumulated other comprehensive (loss) income. On January 1, 2008, the Company derecognized all cash flow hedges. As such, the after-tax net gain of $0.2 million in other comprehensive income at December 31, 2007 will be recognized through operations during 2008.

On December 30, 2004, the Company extinguished $250.0 million of interest rate swaps. These swaps were eliminated at an after-tax gain of $2.6 million. This gain was deferred and was reclassified into operations from accumulated other comprehensive income over three years, which was the original duration of the extinguished swaps. During 2007, 2006 and 2005, $0.1 million, $1.2 million and $1.3 million was recognized in operations, respectively.

The Company recognizes ineffective changes in hedge values resulting from designated SFAS 133 hedges discussed above in the same statement of operations captions as effective changes when such material ineffectiveness occurs. There were no components of derivative instruments that were excluded from the assessment of hedge effectiveness. For 2007, 2006 and 2005, the Company did not recognize any significant gains or losses due to ineffectiveness of its cash flow hedges.

The Company had the following derivative financial instruments (dollars in thousands):

	December 31, 2007		
	Notional Amounts	Fair Value	Expiration Dates
Mortgage Banking Derivatives:			
Rate lock commitments	$3,069,134	$ 26,129	2008
Forward agency and loan sales	3,845,065	(13,504)	2008
Borrowings and advances hedges:			
Interest rate swaps (LIBOR)	130,000	378	2008-2010

	December 31, 2006		
	Notional Amounts	Fair Value	Expiration Dates
Mortgage Banking Derivatives:			
Rate lock commitments	$1,720,879	$3,819	2007
Forward agency and loan sales	2,156,566	4,409	2007
Borrowings and advances hedges:			
Interest rate swaps (LIBOR)	300,000	6,452	2007-2010

Counterparty Credit Risk

The Bank is exposed to credit loss in the event of non-performance by the counterparties to its various derivative financial instruments. The Company manages this risk by selecting only well-established, financially strong counterparties, spreading the credit risk among such counterparties, and by placing contractual limits on the amount of unsecured credit risk from any single counterparty.

Note 25 — Fair Value of Financial Instruments

The Company is required to disclose the fair value information about financial instruments, whether or not recognized in the consolidated statement of financial condition, where it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Because assumptions used in these valuation techniques are inherently subjective in nature, the estimated fair values cannot always be substantiated by comparison to independent market quotes and, in many cases; the estimated fair values could not necessarily be realized in an immediate sale or settlement of the instrument.

The fair value estimates presented herein are based on relevant information available to management as of December 31, 2007 and 2006, respectively. Management is not aware of any factors that would significantly affect these estimated fair value amounts. As these reporting requirements exclude certain financial instruments and all non-financial instruments, the aggregate fair value amounts presented herein do not represent management's estimate of the underlying value of the Company. Additionally, such amounts exclude intangible asset values such as the value of core deposit intangibles.

The following methods and assumptions were used by the Company to estimate the fair value of each class of financial instruments and certain non-financial instruments for which it is practicable to estimate that value:

Cash and cash equivalents. Due to their short term nature, the carrying amount of cash and cash equivalents approximates fair value.

Securities-trading. The carrying amount of the securities trading approximates fair value. Fair value is estimated by discounting future cash flows using assumptions for prepayment rates, market yield requirements and credit losses.

Securities available for sale. The carrying amount of the securities available for sale approximates fair value. Fair value is estimated using quoted market prices or by discounting future cash flows using assumptions for prepayment rates, market yield requirements and credit losses.

Mortgage-backed securities held to maturity. The fair value of mortgage-backed securities is estimated using quoted market prices.

Other investments. The carrying amount of other investments approximates fair value.

Loans receivable. Mortgage loans available for sale and held for investment are valued using fair values attributable to similar mortgage loans. The fair value of the other loans is based on the fair value of obligations with similar credit characteristics.

FHLB stock. No secondary market exists for FHLB stock. The stock is bought and sold at par by the FHLB. Management believes that the recorded value, is the fair value.

Deposit Accounts. The fair value of demand deposits and savings accounts approximates the carrying amount. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for certificates of deposits with similar remaining maturities.

FHLB Advances. Rates currently available to the Company for debt with similar terms and remaining maturities are used to estimate the fair value of the existing debt.

Security Repurchase Agreements. Rates currently available for repurchase agreements with similar terms and maturities are used to estimate fair values for these agreements. For repurchase agreements with maturities that are short term in nature, the carrying amount of the repurchase agreements approximates fair value.

Long Term Debt. The fair value of the long-term debt is estimated based on a discounted cash flow model that incorporates the Company's current borrowing rates for similar types of borrowing arrangements.

Payables for Securities Purchased. Due to their short term nature, the carrying amount of the payables for securities purchased approximates fair value.

Derivative Financial Instruments. The fair value of forward sales contracts, interest rate swaps and fixed-rate commitments to extend credit are based on observable market prices or cash flow projection models acquired from third parties.

The following tables set forth the fair value of the Company's financial instruments (dollars in thousands):

	December 31,			
	2007		2006	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial instruments:				
Assets:				
Cash and cash equivalents	$ 340,169	$ 340,169	$ 277,236	$ 277,236
Securities — trading	13,703	13,703	—	—
Securities available for sale	1,308,608	1,308,608	617,450	617,450
Mortgage-backed securities held to maturity	1,255,431	1,289,083	1,565,420	1,578,382
Other investments	26,813	26,813	24,035	24,035
Loans available for sale	3,511,310	3,543,505	3,188,795	3,212,824
Loans held for investment	8,134,397	8,232,456	8,939,685	10,555,375
FHLB stock	348,944	348,944	277,570	277,570
Liabilities:				
Retail deposits:				
Demand deposits and savings accounts	(1,205,588)	(1,205,588)	(1,132,904)	(1,132,904)
Certificates of deposit	(3,870,828)	(3,890,021)	(3,763,781)	(3,752,959)
Municipal deposits	(1,545,395)	(1,542,530)	(1,419,964)	(1,414,362)
National certificates of deposit	(1,141,549)	(1,154,125)	(1,062,646)	(1,046,768)
FHLB advances	(6,301,000)	(6,397,641)	(5,407,000)	(5,365,825)
Security repurchase agreements	(108,000)	(110,018)	(990,806)	(990,806)
Long term debt	(248,685)	(250,837)	(207,472)	(205,860)
Payables for securities purchased	—	—	(249,694)	(249,694)
Derivative Financial Instruments:				
Forward delivery contracts	(13,504)	(13,504)	4,409	4,409
Commitments to extend credit	26,129	26,129	3,819	3,819
Interest rate swaps	378	378	6,452	6,452

Note 26 — Segment Information

The Company's operations are broken down into two business segments: banking and home lending. Each business operates under the same banking charter but is reported on a segmented basis for this report. Each of the business lines is complementary to each other. The banking operation includes the gathering of deposits and investing those deposits in duration-matched assets primarily originated by the home lending operation. The banking group holds these loans in the investment portfolio in order to earn income based on the difference or "spread" between the interest earned on loans and the interest paid for deposits and other borrowed funds. The home lending operation involves the origination, packaging, and sale of loans in order to receive transaction income. The lending operation also services mortgage loans for others and sells MSRs into the secondary market. Funding for the lending operation is provided by deposits and borrowings garnered by the banking group. All of the non-bank consolidated subsidiaries are included in the banking segment. No such subsidiary is material to the Company's overall operations.

Following is a presentation of financial information by business segment for the period indicated (dollars in thousands):

	As of or for the Year Ended December 31, 2007			
	Banking Operation	Home Lending Operation	Eliminations	Combined
Net interest income	$ 99,984	$ 109,894	$ —	$ 209,878
Net gain on sale revenue	—	64,928	—	64,928
Other income	27,868	24,319	—	52,187
Total net interest income and non-interest income	127,852	199,141	—	326,993
(Loss) earnings before federal income taxes	(74,247)	15,433	—	(58,814)
Depreciation and amortization	13,979	88,986	—	102,965
Capital expenditures	24,318	14,528	—	38,846
Identifiable assets	15,014,734	4,188,002	(3,410,000)	15,792,736
Inter-segment income (expense)	130,808	(130,808)	—	—

	As of or for the Year Ended December 31, 2006			
	Banking Operation	Home Lending Operation	Eliminations	Combined
Net interest income	$ 159,255	$ 55,692	$ —	$ 214,947
Net gain on sale revenue	—	135,002	—	135,002
Other income	31,353	35,806	—	67,159
Total net interest income and non-interest income	190,608	226,500	—	417,108
Earnings before federal income taxes	59,728	56,293	—	116,021
Depreciation and amortization	10,143	86,323	—	96,466
Capital expenditures	43,652	1,704	—	45,356
Identifiable assets	14,939,341	3,597,864	(3,040,000)	15,497,205
Inter-segment income (expense)	80,100	(80,100)	—	—

	As of or for the Year Ended December 31, 2005			
	Banking Operation	Home Lending Operation	Eliminations	Combined
Net interest income	$ 185,276	$ 60,994	$ —	$ 246,270
Net gain on sale revenue	—	81,737	—	81,737
Other income	55,813	21,898	—	77,711
Total net interest income and non-interest income	241,089	164,629	—	405,718
Earnings before federal income taxes	123,726	229	—	123,955
Depreciation and amortization	10,139	115,112	—	125,251
Capital expenditures	32,764	18,633	—	51,397
Identifiable assets	14,176,340	2,379,090	(1,480,000)	15,075,430
Inter-segment income (expense)	42,375	(42,375)	—	—

Revenues are comprised of net interest income (before the provision for loan losses) and non-interest income. Non-interest expenses are fully allocated to each business segment. The intersegment income (expense) consists of interest expense incurred for intersegment borrowing.

Note 27 — (Loss) Earnings Per Share

Basic (loss) earnings per share excludes dilution and is computed by dividing (loss) earnings available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted (loss) earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised and converted into common stock or resulted in the issuance of common stock that could then share in the (loss) earnings of the Company.

The following are reconciliations of the numerator and denominator of the basic and diluted (loss) earnings per share ("EPS") calculation (dollars in thousands, except per share data):

	For the Year Ended December 31, 2007		
	Earnings (Numerator)	Average Shares (Denominator)	Per Share Amount
Basic (loss) earnings	$(39,225)	61,152	$(0.64)
Effect of options	—	357	—
Diluted earnings	$(39,225)	61,509	$(0.64)

In 2007, the Company had 2,376,062 options that were classified as anti-dilutive and were excluded from the EPS calculations.

	For the Year Ended December 31, 2006		
	Earnings (Numerator)	Average Shares (Denominator)	Per Share Amount
Basic earnings	$75,202	63,504	$ 1.18
Effect of options	—	824	(0.01)
Diluted earnings	$75,202	64,328	$ 1.17

In 2006, the Company had 820,582 options that were classified as anti-dilutive and were excluded from the EPS calculations.

	For the Year Ended December 31, 2005		
	Earnings (Numerator)	Average Shares (Denominator)	Per Share Amount
Basic earnings	$79,865	62,128	$ 1.29
Effect of options	—	1,882	(0.04)
Diluted earnings	$79,865	64,010	$ 1.25

In 2005, the Company had 837,449 options that were classified as anti-dilutive and were excluded from the EPS calculations.

Note 28 — Stock-Based Compensation

In 1997, Flagstar's Board of Directors adopted resolutions to implement various stock option and purchase plans and incentive compensation plans in conjunction with the public offering of common stock.

On May 26, 2006, the Company's shareholders approved the Flagstar Bancorp, Inc. 2006 Equity Incentive Plan (the "2006 Plan"). The 2006 Plan consolidates, amends and restates the Company's 1997 Employees and Directors Stock Option Plan, its 2000 Stock Incentive Plan, and its 1997 Incentive Compensation Plan (each, a "Prior Plan"). Awards still outstanding under any of the Prior Plans will continue to be governed by their respective terms. Under the 2006 Plan, key employees, officers, directors and others expected to provide significant services to the Company and its affiliates are eligible to receive awards. Awards that may be granted under the 2006 Plan include stock options, incentive stock options, cash-settled stock appreciation rights, restricted stock units, performance shares and performance units and other awards.

Under the 2006 Plan, the exercise price of any award granted must be at least equal to the fair market value of the Company's common stock on the date of grant. Non-qualified stock options granted to directors expire five years from the date of grant. Grants other than non-qualified stock options have term limits set by the Board of Directors in the applicable agreement. Stock appreciation rights expire seven years from the date of grant unless otherwise provided by the compensation committee of the Board of Directors.

In December 2004, the FASB issued SFAS 123R (revised 2004), *Share-Based Payment*, ("SFAS 123R") which requires that compensation costs related to share-based payment transactions be recognized in financial statements. SFAS 123R eliminated the alternative to use the intrinsic method of accounting previously allowed under APB 25, *Accounting for Stock Issued to Employees*, which generally did not require any compensation expense to be recognized in the financial statements for the grant of stock options to employees if certain conditions were met. Only certain pro forma disclosures of share-based payments were required.

On January 1, 2006, the Company adopted SFAS 123R using the modified prospective method. SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized as expense in the consolidated statement of earnings based on their fair values. The amount of compensation expense is determined based on the fair value of the options when granted and is expensed over the required service period, which is normally the vesting period of the options. SFAS 123R applies to awards granted or modified on or after January 1, 2006, and to any unvested awards that were outstanding at December 31, 2005. Consequently, compensation expense is recorded for prior option grants that vest on or after January 1, 2006, the date of adoption.

Prior to the adoption of SFAS 123R, the Company accounted for its Prior Plans under the recognition and measurement principles of APB 25. The Company reported all tax benefits resulting from the exercise of stock options as financing cash flows in the consolidated statements of cash flows. In accordance with SFAS 123R, for the period beginning January 1, 2006, only the excess tax benefits from the exercise of stock options are presented as financing cash flows. The excess tax benefits totaled $(25,000) and $1.0 million for the years ended December 31, 2007 and 2006, respectively.

The fair value concepts were not changed significantly in SFAS 123R; however, in adopting this standard, companies must choose among alternative valuation models and amortization assumptions. The Company has elected to continue to use both the Black-Scholes option pricing model and the straight-line method of amortization of compensation expense over the requisite service period of the grant. The Company will reconsider use of the Black-Scholes model if additional information in the future indicates another model would be more appropriate at that time or if grants issued in future periods have characteristics that could not be reasonably estimated using this model.

During 2007 and 2006, compensation expense recognized related to the 2006 Plan totaled $1.3 million and $2.2 million, respectively.

Stock Option Plan

The following tables summarize the activity that occurred in the years ended December 31:

	Number of Shares		
	2007	2006	2005
Options outstanding, beginning of year	3,029,737	3,417,366	4,961,529
Options granted	—	—	372,792
Options exercised	(15,440)	(359,503)	(1,788,354)
Options canceled, forfeited and expired	(316,300)	(28,126)	(128,601)
Options outstanding, end of year	2,697,997	3,029,737	3,417,366
Options exercisable, end of year	2,694,747	2,885,787	2,861,884

The total intrinsic value of options exercised during the years ended December 31, 2007, 2006 and 2005 was $0.1 million, $3.2 million and $23.9 million, respectively. Additionally, the aggregate intrinsic value of options outstanding and exercisable at December 31, 2007 was $1.0 million and $1.0 million, respectively.

	Weighted Average Exercise Price		
	2007	2006	2005
Options outstanding, beginning of year	$13.79	$13.02	$ 9.34
Options granted	—	—	20.50
Options exercised	4.46	6.13	4.17
Options canceled, forfeited and expired	12.08	18.30	15.64
Options outstanding, end of year	$14.04	$13.79	$13.02
Options exercisable, end of year	$14.04	$13.86	$13.20

The following information pertains to the stock options issued pursuant to the Prior Plans, but not exercised at December 31, 2007:

	Options Outstanding			Options Exercisable	
Range of Grant Price	Number of Options Outstanding at December 31, 2007	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable at December 31, 2007	Weighted Average Exercise Price
$ 1.76 - 1.96	132,509	2.50	$ 1.78	132,509	$ 1.78
4.32 - 4.77	15,000	0.29	4.48	15,000	4.48
5.01 - 6.06	174,426	2.36	5.19	174,426	5.19
11.80 - 12.27	1,563,380	3.95	12.03	1,563,380	12.03
15.23	9,500	6.34	15.23	6,250	15.23
19.35 - 19.42	18,429	5.18	19.38	18,429	19.38
20.02 - 20.73	357,863	5.41	20.69	357,863	20.69
22.68 - 24.72	426,890	5.83	23.36	426,890	23.36
	2,697,997		$14.04	2,694,747	$14.04

At December 31, 2007, options available for future grants were 1,295,809. Shares issued under the 2006 Plan may consist, in whole or in part, of authorized and unissued shares or treasury shares. The Company does not expect a material cash outlay relating to obtaining shares expected to be issued under the 2006 Plan during 2008.

The following table illustrates the effect on net earnings and earnings per share as of and for the year ended December 31, 2005 as if the Company had applied the fair value recognition provision of SFAS No. 123R to stock-based employee compensation (dollars in thousands except per share data):

	For the Year Ended December 31, 2005
Net earnings	$79,865
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	4,540
Pro forma net earnings	$75,325
Basic earnings per share	
As reported	$ 1.29
Pro forma	$ 1.21
Diluted earnings per share	
As reported	$ 1.25
Pro forma	$ 1.18

The fair value of each option grant is estimated using the Black-Scholes options-pricing model with the following weighted average assumptions used for grants in 2005: dividend yield of 4.80%; expected volatility of 45.28%; a risk-free rate of 3.80%; an expected life of 5 years; and a fair value per option of $5.86.

During the fourth quarter of 2005, the Company accelerated the vesting of its unvested and "out-of-the-money" stock options awarded to its employees, executive members and board members under its stock option plan. The acceleration applied only to unvested options with an exercise price of $19.35 per share or higher. The options considered to be "out-of-the-money" had exercise prices greater than the Company's stock closing sales price on November 29, 2005, which was $15.20 per share. Outstanding unvested options that were "in-the-money" were not subject to acceleration and will continue to vest on their normal schedule. As a result of the acceleration, options to purchase 829,899 shares of Flagstar common stock, which would otherwise have vested over the next four years, became fully vested. These options represented approximately 24% of the then total options outstanding. The total weighted average exercise price per share was $22.16 for these options.

Cash-settled Stock Appreciation Rights

The Company issues cash-settled stock appreciation rights ("SAR") to officers and key employees in connection with year-end compensation. Cash-settled stock appreciation rights generally vest 25% of the grant on each of the first four anniversaries of the grant date. The standard term of a SAR is seven years beginning on the grant date. Grants of SARs will be settled only in cash and once made, a grant of a SAR which will be settled only in cash may not be later amended or modified to be settled in common stock or a combination of common stock and cash.

The Company used the following weighted average assumptions in applying the Black-Scholes model to determine the fair value of the cash-settled stock appreciation rights it issued during the year ended December 31, 2007: dividend yield of 2.9%; expected volatility of 44.2%; a risk-free rate of 3.3%; and an expected life of five years. For the year ended December 31, 2006; dividend yield of 3.68%; expected volatility of 21.98%; a risk-free rate of 4.99%; and an expected life of five years.

The following table presents the status and changes in cash-settled stock appreciation rights issued under the 2006 Plan:

	Shares	Weighted Average Exercise Price	Grant Date Fair Value
Stock Appreciation Rights Awarded:			
Non-vested balance at December 31, 2006	328,873	$16.28	$2.99
Granted	590,692	14.34	1.43
Vested	(82,197)	16.28	2.99
Forfeited	(14,569)	14.90	1.76
Non-vested balance at December 31, 2007	822,799	14.91	1.89

The Company incurred expense of $42,000 ($27,000 net of tax) and $168,000 ($109,000 net of tax) with respect to cash-settled stock appreciation rights during 2007 and 2006, respectively. At December 31, 2007, the non-vested cash settled stock appreciation rights have a total compensation cost of approximately $1.6 million expected to be recognized over the weighted average remaining vesting period of approximately three years.

Restricted Stock Units

The Company issues restricted stock units to officers, directors and key employees in connection with year-end compensation. Restricted stock generally will vest in 50% increments on each annual anniversary of the date of grant beginning with the first anniversary. At December 31, 2007, the maximum number of shares of common stock that may be issued under the 2006 Plan as the result of any grants is 1,224,997 shares. The Company incurred expenses of approximately $1.1 million, $446,000, and $2.9 million with respect to restricted stock units, during 2007, 2006 and 2005, respectively. As of December 31, 2007, restricted stock units had a market value of $0.9 million.

	Shares	Weighted Average Grant-Date Fair Value per Share
Restricted Stock:		
Nonvested at December 31, 2006	98,459	$16.93
Granted	91,381	14.30
Vested	(63,792)	16.81
Canceled and forfeited	(2,373)	14.89
Nonvested at December 31, 2007	123,675	14.29

Stock Purchase Plan

Under the Employee Stock Purchase Plan ("Purchase Plan"), eligible participants, upon providing evidence of a purchase of the Company's common shares from any third party on the open market, receive a payment from the Company equal to 15% of the share price. The Purchase Plan includes limitations on the maximum reimbursement to a participant during a year. The Purchase Plan has not been designed to comply with the requirements of the Internal Revenue Code with respect to employee stock purchase plans. During 2005, the Company incurred expenses of approximately $82,100 under the Purchase Plan. This Purchase Plan was terminated as of December 31, 2005.

Incentive Compensation Plan

The Incentive Compensation Plan ("Incentive Plan") is administered by the compensation committee of the Board of Directors. Each year the committee decides which employees of the Company will be eligible to participate in the Incentive Plan and the size of the bonus pool. During 2007, 2006 and 2005, all members of the executive management team were included in the Incentive Plan. The Company incurred expenses of $4.8 million, $2.2 million, and $2.2 million on the Incentive Plan for the years ended December 31, 2007, 2006 and 2005, respectively.

Note 29 — Quarterly Financial Data (Unaudited)

The following table represents summarized data for each of the quarters in 2007, 2006, and 2005 (dollars in thousands, except (loss) earnings per share data) certain per share results have been adjusted to conform to the 2007 presentation:

	2007			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$220,570	$222,464	$237,151	$225,324
Interest expense	168,598	172,547	183,215	171,271
Net interest income	51,972	49,917	53,936	54,053
Provision for loan losses	8,293	11,452	30,195	38,357
Net interest income after provision for loan losses	43,679	38,465	23,741	15,696
Loan administration	2,615	3,149	4,333	2,618
Net gain (loss) on loan sales	25,154	28,144	(17,457)	23,189
Net gain (loss) on MSR sales	115	5,610	456	(283)
Other non-interest income (loss)	12,014	20,541	13,936	(7,019)
Non-interest expense	71,398	72,234	73,260	80,618
(Loss) earnings before federal income tax provision	12,179	23,675	(48,251)	(46,417)
(Benefit) provision for federal income taxes	4,420	8,544	(16,196)	(16,357)
Net (loss) earnings	$ 7,759	$ 15,131	$ (32,055)	$ (30,060)
Basic (loss) earnings per share	$ 0.12	$ 0.25	$ (0.53)	$ (0.50)
Diluted (loss) earnings per share	$ 0.12	$ 0.25	$ (0.53)	$ (0.50)

Flagstar Bancorp, Inc.
Notes to the Consolidated Financial Statements - continued

	2006			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$191,299	$192,648	$205,557	$211,362
Interest expense	132,624	141,910	151,929	159,456
Net interest income	58,675	50,738	53,628	51,906
Provision for loan losses	4,063	5,859	7,291	8,237
Net interest income after provision for loan losses	54,612	44,879	46,337	43,669
Loan administration	4,355	309	7,766	602
Net gain on loan sales	17,084	9,650	(8,197)	23,844
Net gain on MSR sales	8,586	34,932	45,202	3,901
Other non-interest income	12,596	16,681	9,567	15,283
Non-interest expense	68,070	62,354	68,853	76,360
Earning before federal income tax provision	29,163	44,097	31,822	10,939
Provision for federal income taxes	10,253	15,457	11,070	4,039
Net earnings	$ 18,910	$ 28,640	$ 20,752	$ 6,900
Basic earnings per share	$ 0.30	$ 0.45	$ 0.33	$ 0.11
Diluted earnings per share	$ 0.29	$ 0.44	$ 0.32	$ 0.11

	2005			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$163,125	$166,111	$185,391	$194,035
Interest expense	97,916	107,670	124,617	132,191
Net interest income	65,209	58,441	60,774	61,844
Provision for loan losses	6,246	2,903	3,690	6,036
Net interest income after provision for loan losses	58,963	55,538	57,084	55,808
Loan administration	5,945	1,669	(1,913)	3,060
Net gain on loan sales	9,577	32,348	3,426	18,229
Net gain on MSR sales	4,248	2,262	492	11,155
Other non-interest income	15,792	18,590	18,763	15,806
Non-interest expense	63,723	67,074	63,229	68,862
Earnings before federal income tax provision	30,802	43,333	14,623	35,196
Provision for federal income taxes	11,024	15,533	5,163	12,369
Net earnings	$ 19,778	$ 27,800	$ 9,460	$ 22,827
Basic earnings per share	$ 0.32	$ 0.45	$ 0.15	$ 0.36
Diluted earnings per share	$ 0.31	$ 0.43	$ 0.15	$ 0.36

Note 30 — Holding Company Only Financial Statements

The following are unconsolidated financial statements for the Company. These condensed financial statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto:

Flagstar Bancorp, Inc.
Condensed Unconsolidated Statements of Financial Condition
(Dollars in thousands)

	December 31, 2007	December 31, 2006
Assets		
Cash and cash equivalents	$ 4,314	$ 4,393
Investment in subsidiaries	936,613	1,013,390
Other assets	1,980	3,011
Total assets	$942,907	$1,020,794
Liabilities and Stockholders' Equity Liabilities		
Long term debt	$247,435	$ 206,197
Total interest paying liabilities	247,435	206,197
Other liabilities	2,494	2,363
Total liabilities	249,929	208,560
Stockholders' Equity		
Common stock	637	636
Additional paid in capital	64,350	63,223
Accumulated other comprehensive income	(11,495)	5,182
Retained earnings	681,165	743,193
Treasury stock	(41,679)	—
Total stockholders' equity	692,978	812,234
Total liabilities and stockholders' equity	$942,907	$1,020,794

Flagstar Bancorp, Inc.
Condensed Unconsolidated Statements of Earnings
(Dollars in thousands)

	For the Years Ended December 31,		
	2007	2006	2005
Income			
Dividends from subsidiaries	$ 68,314	$46,250	$22,200
Interest	497	450	335
Total	68,811	46,700	22,535
Expenses			
Interest	15,289	13,833	10,662
Other taxes	(148)	(179)	—
General and administrative	2,062	1,981	2,015
Total	17,203	15,635	12,677
Earnings before undistributed (loss) earnings of subsidiaries	51,608	31,065	9,858
Equity in undistributed (loss) earnings of subsidiaries	(96,680)	38,822	65,695
(Loss) earnings before federal income tax benefit	(45,072)	69,887	75,553
Federal income tax benefit	(5,847)	(5,315)	(4,312)
Net (loss) earnings	$(39,225)	$75,202	$79,865

Flagstar Bancorp, Inc.
Condensed Unconsolidated Statements of Cash Flows
(Dollars in thousands)

	For the Years Ended December 31,		
	2007	2006	2005
Operating Activities			
Net (loss) earnings	$(39,225)	$ 75,202	$ 79,865
Adjustments to reconcile net (loss) earnings to net cash provided by operating activities			
Equity in undistributed earnings of subsidiaries	96,680	(38,822)	(65,695)
Stock-based compensation	1,083	2,718	745
Change in other assets	(259)	669	(667)
Provision for deferred tax benefit	(447)	(120)	—
Change in other liabilities	2,453	(9,412)	11,043
Net cash provided by operating activities	60,285	30,235	25,291
Investing Activities			
Net change in other investments	12	11	11
Net change in investment in subsidiaries	(38,605)	(3,766)	(77,719)
Net cash used in investment activities	(38,593)	(3,755)	(77,708)
Financing Activities			
Proceeds from the issuance of junior subordinated debentures	41,238	—	103,095
Proceeds from exercise of stock options and grants issued	70	2,205	7,444
Tax benefit from stock options exercised	(25)	1,000	8,379
Purchase of treasury stock	(41,705)	—	—
Issuance of treasury stock	26	—	—
Dividends paid	(21,375)	(38,122)	(55,995)
Net cash (used in) provided by financing activities	(21,771)	(34,917)	62,923
Net increase (decrease) in cash and cash equivalents	(79)	(8,437)	10,506
Cash and cash equivalents, beginning of year	4,393	12,830	2,324
Cash and cash equivalents, end of year	$ 4,314	$ 4,393	$ 12,830

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES

None.

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

We are responsible for establishing and maintaining disclosure controls and procedures, as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 as amended (the Exchange Act), that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is: (a) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms; and (b) accumulated and communicated to our management, including our principal executive and principal financial officers, to allow timely decisions regarding required disclosures. In designing and evaluating our disclosure controls and procedures, we recognize that any controls and procedures, no matter how well designed and implemented, can provide only reasonable assurance of achieving the desired control objectives, and that our management's duties require it to make its best judgment regarding the design of our disclosure controls and procedures.

As of December 31, 2007, we conducted an evaluation, under the supervision (and with the participation) of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to the Exchange Act. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were operating effectively.

Management's Report on Internal Control Over Financial Reporting

Our management, under the supervision of our Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rule 13a-15(f) under the Exchange Act. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. GAAP. Internal control over financial reporting includes policies and procedures that:

(i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;

(ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of the financial statements in accordance with U.S. GAAP, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and

(iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with existing policies or procedures may deteriorate.

Under the supervision of our Chief Executive Officer and Chief Financial Officer, our management conducted an assessment of our internal control over financial reporting as of December 31, 2007, based on the framework and criteria established in *Internal Control-Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Based on this assessment, we assert that, as of December 31, 2007 and based on the specific criteria, the Company maintained effective internal control over financial reporting, involving the preparation and reporting of the Company's consolidated financial statements presented in uniformity with U.S. GAAP.

Management's assessment of the effectiveness of our internal control over financial reporting as of December 31, 2007, has been audited by Virchow, Krause & Company, LLP, our independent registered public accounting firm, as stated in their report, which is included herein.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS OF THE REGISTRANT AND CORPORATE GOVERNANCE

The information required by this Item 10 is hereby incorporated by reference to the Company's Proxy Statement for the Company's 2008 Annual Meeting of Stockholders (the "Proxy Statement"), to be filed pursuant to Regulation 14A within 120 days after the end of our 2007 fiscal year.

We have adopted a Code of Business Conduct and Ethics that applies to our employees, officers and directors, including our principal executive officer, principal financial officer, and principal accounting officer. Our Code of Business Conduct and Ethics can be found on our web site, which is located at www.flagstar.com. We intend to make all required disclosures concerning any amendments to, or waivers from, our Code of Business Conduct and Ethics on our website.

We have also adopted Corporate Governance Guidelines and charters for the Audit Committee, Compensation Committee, and Nominating Corporate Governance Committee and copies are available at http://www.flagstar.com or upon written request for stockholders to Flagstar Bancorp, Inc., Attn: Paul Borja, CFO, 5151 Corporate Drive, Troy, MI 48098.

None of the information currently posted, or posted in the future, on our website is incorporated by reference into this Form 10-K.

In 2007, the Company's Chief Executive Officer provided to the NYSE the Annual CEO Certification regarding the Company's compliance with the NYSE's corporate governance listing standards as required by Section 303A-12(a) of the NYSE Listed Company Manual. In addition, the Company has filed as exhibits to this annual report on Form 10-K for the year ended December 31, 2007, the applicable certifications of its Chief Executive Officer and its Chief Financial Officer required under Section 302 of the Sarbanes-Oxley Act of 2002 regarding the quality of the Company's public disclosures.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item 11 is hereby incorporated by reference to the Company's Proxy Statement, to be filed pursuant to Regulation 14A within 120 days after the end of our 2007 fiscal year.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this Item 12 is hereby incorporated by reference to the Company's Proxy Statement, to be filed pursuant to Regulation 14A within 120 days after the end of our 2007 fiscal year. Reference is also made to the information appearing in "Market for the Registrant's Common Equity and Related Stockholder Matters" under Item 5 of this Form 10-K, which is incorporated herein by, reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information required by this Item 13 is hereby incorporated by reference to the Company's Proxy Statement, to be filed pursuant to Regulation 14A within 120 days after the end of our 2007 fiscal year.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this Item 14 is hereby incorporated by reference to the Company's Proxy Statement, to be filed pursuant to Regulation 14A within 120 days after the end of our 2007 fiscal year.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a)(1) and (2) — Financial Statements and Schedules

The information required by these sections of Item 15 are set forth in the Index to Consolidated Financial Statements under Item 8 of this annual report on Form 10-K.

(3) — Exhibits

The following documents are filed as a part of, or incorporated by reference into, this report:

Exhibit No.	Description
3.1*	Second Restated Articles of Incorporation of the Company (previously filed as Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q, dated August 4, 2006, and incorporated herein by reference).
3.2*	Fourth Amended and Restated Bylaws of the Company (previously filed as Exhibit 3.1 to the Company's Current Report on Form 8-K, dated February 29, 2008, and incorporated herein by reference).
10.1*+	Employment Agreement, dated as of February 28, 2007, between the Company, Flagstar Bank, FSB, and Thomas J. Hammond (previously filed as Exhibit 10.1 to the Company's Annual Report on Form 10-K, dated February 28, 2007 and incorporated herein by reference).
10.2*+	Employment Agreement, dated as of February 28, 2007, between the Company, Flagstar Bank, FSB, and Mark T. Hammond (previously filed as Exhibit 10.2 to the Company's Annual Report on Form 10-K, dated February 28, 2007 and incorporated herein by reference).
10.3*+	Employment Agreement, dated as of February 28, 2007, between the Company, Flagstar Bank, FSB, and Paul D. Borja (previously filed as Exhibit 10.3 to the Company's Annual Report on Form 10-K, dated February 28, 2007 and incorporated herein by reference).
10.4*+	Employment Agreement, dated as of February 28, 2007, between the Company, Flagstar Bank, FSB, and Kirstin A. Hammond (previously filed as Exhibit 10.4 to the Company's Annual Report on Form 10-K, dated February 28, 2007 and incorporated herein by reference).
10.5*+	Employment Agreement, dated as of February 28, 2007, between the Company, Flagstar Bank, FSB, and Robert O. Rondeau, Jr. (previously filed as Exhibit 10.5 to the Company's Annual Report on Form 10-K, dated February 28, 2007 and incorporated herein by reference).
10.6*+	Flagstar Bancorp, Inc. 1997 Employees and Directors Stock Option Plan as amended (previously filed as Exhibit 4.1 to the Company's Form S-8 Registration Statement (No. 333-125513), dated June 3, 2005, and incorporated herein by reference).
10.7*+	Flagstar Bank 401(k) Plan (previously filed as Exhibit 4.1 to the Company's Form S-8 Registration Statement (No. 333-77501), dated April 30, 1999, and incorporated herein by reference).
10.8*+	Flagstar Bancorp, Inc. 2000 Stock Incentive Plan as amended (previously filed as Exhibit 4.1 to the Company's Form S-8 Registration Statement (No. 333-125512), dated June 3, 2005, and incorporated herein by reference).
10.9*+	Flagstar Bancorp, Inc. Incentive Compensation Plan (previously filed as Exhibit 10.4 to the Company's Form S-1 Registration Statement (No. 333-21621) and incorporated herein by reference).
10.10*+	Flagstar Bancorp, Inc. 2006 Equity Incentive Plan (previously filed as Exhibit 10.1 to the Company's Current Report on Form 8-K, dated March 26, 2006, and incorporated herein by reference).

Exhibit No.	Description
10.11+	Employment Agreement, dated as of February 28, 2007, between the Company, FlagstarBank, FSB, and Matthew I. Roslin.
11	Statement regarding computation of per share earnings incorporated by reference to 27 of the Notes to Consolidated Financial Statements of this report.
14*	Flagstar Bancorp, Inc. Code of Business Conduct and Ethics (previously filed as Exhibit 14 to the Company's Annual Report on Form 10-K, dated March 16, 2006, and incorporated herein by reference)
21	List of Subsidiaries of the Company.
23	Consent of Virchow, Krause & Company, LLP
31.1	Section 302 Certification of Chief Executive Officer
31.2	Section 302 Certification of Chief Financial Officer
32.1	Section 906 Certification of Chief Executive Officer
32.2	Section 906 Certification of Chief Financial Officer

* Incorporated herein by reference

\+ Constitutes a management contract or compensation plan or arrangement

Flagstar Bancorp, Inc., will furnish to any stockholder a copy of any of the exhibits listed above upon written request and upon payment of a specified reasonable fee, which fee shall be equal to the Company's reasonable expenses in furnishing the exhibit to the stockholder. Requests for exhibits and information regarding the applicable fee should be directed to "Paul Borja, CFO" at the address of the principal executive offices set forth on the cover of this Annual Report on Form 10-K.

(b) — Exhibits. See Item 15(a)(3) above.

(c) — Financial Statement Schedules. See Item 15(a)(2) above.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on March 13, 2008.

FLAGSTAR BANCORP, INC.

By: /s/ MARK T. HAMMOND

Mark T. Hammond
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on March 13, 2008.

	SIGNATURE	TITLE
By:	/s/ THOMAS J. HAMMOND Thomas J. Hammond	Chairman of the Board
By:	/s/ MARK T. HAMMOND Mark T. Hammond	Vice Chairman of the Board, President, and Chief Executive Officer (Principal Executive Officer)
By:	/s/ PAUL D. BORJA Paul D. Borja	Executive Vice-President and Chief Financial Officer (Principal Financial and Accounting Officer)
By:	/s/ KIRSTIN A. HAMMOND Kirstin A. Hammond	Executive Director and Director
By:	/s/ ROBERT O. RONDEAU, JR. Robert O. Rondeau, JR.	Executive Director and Director
By:	/s/ CHARLES BAZZY Charles Bazzy	Director
By:	/s/ JAMES D. COLEMAN James D. Coleman	Director
By:	/s/ RICHARD S. ELSEA Richard S. Elsea	Director
By:	/s/ MICHAEL LUCCI SR Michael Lucci Sr.	Director
By:	/s/ ROBERT W. DEWITT Robert W. Dewitt	Director
By:	/s/ FRANK D’ANGELO Frank D’Angelo	Director
By:	/s/ B. BRIAN TAUBER B. Brian Tauber	Director
By:	/s/ JAY J. HANSEN Jay J. Hansen	Director
By:	/s/ WILLIAM F. PICKARD William F. Pickard	Director

EXHIBIT INDEX

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\+ Constitutes a management contract or compensation plan or arrangement

NATIONAL HEADQUARTERS
Troy, Mich.

Flagstar®
Bancorp

NATIONAL HEADQUARTERS
5151 CORPORATE DRIVE, TROY, MI 48098 ★ (800) 945-7700 ★ WWW.FLAGSTAR.COM