



*Federal Deposit Insurance Corporation*  
*Annual Report 2006*

**FDIC**



# Annual

## Mission

In its unique role as deposit insurer of banks and savings associations, and in cooperation with the other state and federal regulatory agencies, the **Federal Deposit Insurance Corporation (FDIC)** promotes the safety and soundness of the U.S. financial system and the insured depository institutions by identifying, monitoring and addressing risks to the deposit insurance fund.

The FDIC promotes public understanding and the development of sound public policy by providing timely and accurate financial and economic information and analyses. It minimizes disruptive effects from the failure of banks and savings associations. It assures fairness in the sale of financial products and the provision of financial services.

The FDIC's long and continuing tradition of excellence in public service is supported and sustained by a highly skilled and diverse workforce that continuously monitors and responds rapidly and successfully to changes in the financial environment.

The Federal Deposit Insurance Corporation (FDIC) is an independent agency created by the Congress that maintains the stability and public confidence in the nation's financial system by insuring deposits, examining and supervising financial institutions, and managing receiverships.

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# Report 2006

## **Vision**

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The FDIC is a leader in developing and implementing sound public policies, identifying and addressing new and existing risks in the nation's financial system, and effectively and efficiently carrying out its insurance, supervisory, and receivership management responsibilities.

## **Values**

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The FDIC and its employees have a long and continuing tradition of distinguished public service. Six core values guide FDIC employees as they strive to fulfill the Corporation's mission and vision:

### **Integrity**

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FDIC employees adhere to the highest ethical standards in the performance of their duties and responsibilities.

### **Competence**

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The FDIC maintains a highly skilled, dedicated, and diverse workforce.

### **Teamwork**

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FDIC employees work cooperatively with one another and with employees in other regulatory agencies to accomplish the Corporation's mission.

### **Effectiveness**

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The FDIC responds quickly and successfully to identified risks in insured financial institutions and in the broader financial system.

### **Financial Stewardship**

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The FDIC acts as a responsible fiduciary, consistently operating in an efficient and cost-effective manner on behalf of insured financial institutions and other stakeholders.

### **Fairness**

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The FDIC treats all employees, insured financial institutions, and other stakeholders with impartiality and mutual respect.



**Federal Deposit Insurance Corporation**  
550 17th Street, NW Washington, DC 20429

Office of the Chairman

February 15, 2007

Dear Sir/Madam,

In accordance with:

- the provisions of section 17(a) of the Federal Deposit Insurance Act,
- the Chief Financial Officers Act of 1990, Public Law 101-576,
- the Government Performance and Results Act of 1993,
- the provisions of Section 5 (as amended) of the Inspector General Act of 1978, and
- the Reports Consolidation Act of 2000,

the Federal Deposit Insurance Corporation (FDIC) is pleased to submit its 2006 Annual Report (also referred to as the Performance and Accountability Report), which includes the audited financial statements of the Deposit Insurance Fund and the Federal Savings and Loan Insurance Corporation Resolution Fund.

In accordance with the Reports Consolidation Act of 2000, the FDIC completed an assessment of the reliability of the performance data contained in this report. No material inadequacies were found and the data are considered to be complete and reliable.

Based on internal management evaluations, and in conjunction with the results of independent financial statement audits, the FDIC can provide reasonable assurance that the objectives of Section 2 (internal controls) and Section 4 (financial management systems) of the Federal Managers' Financial Integrity Act of 1982 have been achieved, and that the FDIC has no material weaknesses. Additionally, the U.S. Government Accountability Office did not identify any significant deficiencies in the FDIC's internal controls for 2006. We are committed to maintaining our effective internal controls corporate-wide in 2007.

Sincerely,

**Sheila C. Bair**  
Chairman

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The President of the United States  
The President of the United States Senate  
The Speaker of the United States House of Representatives

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## Message from the Chairman • Sheila C. Bair



I am pleased to present the Federal Deposit Insurance Corporation's (FDIC) 2006 Annual Report (also referred to as the Performance and Accountability Report). The condition of the banking and thrift industry continues to be healthy and profitable and 2006 saw continuation of the longest period in the Corporation's 73-year history without a failure of an FDIC-insured institution—a record 31 months. Nevertheless, we continued in 2006 to actively pursue our mission of ensuring the stability of and public confidence in the nation's financial system.

The past year was a particularly significant one for the FDIC. On February 8, 2006, President Bush signed into law the Federal Deposit Insurance Reform Act of 2005, culminating a lengthy, multi-year effort by the FDIC, the Administration, and the Congress to make sweeping improvements to the federal deposit insurance system. The law requires the FDIC to make fundamental changes in its deposit insurance policies and business processes in 2006 and 2007, and we are well on our way toward full compliance with the provisions of that Act.

We focused much of our attention during 2006 on three high priority areas of activity: (1) addressing significant policy issues, (2) maintaining a strong supervisory program, and (3) concentrating our efforts on promoting economic inclusion. I would like to share with you some of our major successes during 2006 and some of our challenges for 2007 and beyond.

### Policy Challenges

In accordance with the requirements of the deposit insurance reform statute, the FDIC in early 2006 merged the Bank Insurance Fund and the Savings Association Insurance Fund into the new Deposit Insurance Fund, and adopted new regulations increasing coverage for certain retirement plan deposits from \$100,000 to \$250,000. This was the first major change in deposit insurance coverage since 1980. The reform statute also provided the FDIC Board of Directors (Board) with greater flexibility to manage the Deposit Insurance Fund. The Board adopted final rules on a new assessment system that will make assessments more risk-sensitive and distribute the assessment burden more fairly across insured institutions, and it established new premium rates effective for deposit insurance beginning January 1, 2007. In addition, the Board adopted final rules on the distribution and use of \$4.7 billion in one-time assessment credits, a temporary plan for the allocation of future dividends, and a designated reserve ratio. In 2007, the FDIC will complete and issue guidance on how limited adjustments may be made in the pricing of deposit insurance for large banks and publish an advance notice of proposed rulemaking seeking comment about how to implement a permanent dividend system.

Capital reform was a major area of focus in 2006. The FDIC continued to work with the other federal regulators and to participate actively on the Basel Committee on Banking Supervision, and many of its subgroups, in planning for the implementation of the new Basel II capital framework. The Board approved in September 2006 the publication of a notice of proposed rulemaking (NPR), jointly with the Federal Reserve Board, the Office of the Comptroller of the Currency and the Office of Thrift Supervision, seeking comment on draft regulations to implement the advanced approaches of the Basel II Accord. As a result of the findings in the fourth quantitative impact study (QIS-4), which

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examined the potential impact that the Basel II capital framework might have on the minimum risk-based capital requirements of a select group of financial institutions, safeguards were incorporated into the Basel II NPR to protect against an unacceptable decline in minimum risk-based capital requirements.

On December 5, 2006, the Board also approved the publication of a second NPR seeking comment on draft regulations to implement a new capital framework, referred to as Basel IA, which banks that do not use the Basel II capital framework may opt to apply. The Basel IA NPR was also issued jointly with the Federal Reserve Board, the Office of the Comptroller of the Currency and the Office of Thrift Supervision.

Both draft regulations represent an effort to enhance the risk sensitivity of the existing risk-based capital framework while maintaining safety and soundness within the banking and thrift industry. Throughout the interagency deliberations on both Basel II and Basel IA, the FDIC has maintained an unwavering commitment to the maintenance of strong capital requirements and to the principle that any changes to these requirements should have a minimal impact on competitive equity among banks of all sizes. In 2007, the FDIC will continue to provide leadership in this effort. It will explore the potential of using simplified approaches as an alternative to the advanced approaches in the Basel II Accord and, with the other banking agencies, work to achieve consensus on the overall package of regulatory capital changes for final publication.

Another significant policy challenge is presented by the continuing consolidation in the banking industry. While this presents challenges for all federal banking regulators, it poses unique issues for the FDIC because of its multiple roles as regulator, deposit insurer, and receiver. Fortunately, the banking industry and our largest banks are strong and have made many improvements to their risk management processes in recent years. Even so, the FDIC must be prepared to respond to instability in any size insured institution. To meet these challenges, the FDIC continues to enhance its capabilities to protect insured depositors and maintain stability in our banking system. Some of the initiatives involved in this ongoing process are contingency planning exercises, system and process improvements for determination of deposit insurance claims and management of failing bank assets, consultations with domestic and international regulators, improvements to the FDIC's supervisory program for larger banks, and the designation of internal and external expertise to focus on larger bank issues. This effort will continue and evolve as the challenges change in the future.

Matters that received significant public interest in 2006 included applications to the FDIC for deposit insurance filed by commercial companies for proposed industrial loan companies (ILCs). To obtain the public's insight on the issues, on July 28, 2006, the FDIC placed a six-month moratorium, ending on January 31, 2007, on ILC deposit insurance applications and change in control notices to give the FDIC time to assess developments in the ILC industry; to determine whether any emerging safety and soundness or policy issues exist; and to evaluate whether statutory, regulatory or policy changes need to be made in the oversight of these institutions. The moratorium also allowed FDIC time to further evaluate the various issues, facts and arguments raised in connection

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with the ILC industry, and to assess whether statutory or regulatory changes or revised standards and procedures for ILC applications and supervision are needed to protect the Deposit Insurance Fund or important Congressional objectives. In August, the FDIC Board requested public comment on a broad range of ILC-related issues. During the 45-day comment period that ended on October 10, 2006, we received more than 12,600 comments which were carefully and thoroughly evaluated.

### **Supervisory Program**

In addition to managing an unusually large policy agenda, the FDIC also continued to administer strong and effective supervisory programs in 2006 in both the risk management and compliance areas. The FDIC performed 2,388 safety and soundness examinations, 1,959 compliance and Community Reinvestment Act exams and 3,052 specialty exams.

During the year, the FDIC enhanced the quality of fair lending examinations through the use of residential mortgage pricing data. This year represented the first opportunity for the FDIC to use pricing data collected by financial institutions pursuant to the 2004 changes to the Home Mortgage Disclosure Act. Also in 2006, the FDIC established the Large Bank Program to address challenges associated with supervising and insuring the deposits of large and complex institutions. In addition, the FDIC completed and issued guidance on concentrations in commercial real estate. This guidance provides supervisory criteria to assist in identifying institutions with significant concentrations of commercial real estate.

Further, the FDIC became increasingly concerned with the expansion of nontraditional mortgage products and the potential risk posed by these products to the DIF. To address these concerns, the FDIC implemented certain enhancements to the supervisory oversight of nontraditional mortgage banking activities and, with the other financial institution regulatory agencies, developed and issued guidance to address the growing risks in these loan products.

During the year, the FDIC conducted a comprehensive review of the compliance examination program's workload and resources. Based on workload projections, we identified the need for additional staffing in this area. In December, the Board authorized 72 new examiner positions to be phased in over a three-year period with the majority added in 2007. This will result in an increase of human resources dedicated to the compliance and CRA examination areas.

Reflecting our commitment to provide current and consistent guidance for examiners and banking organizations to comply with the Bank Secrecy Act (BSA) and Anti-Money Laundering (AML) requirements, we worked closely with the other federal banking regulators to revise the Federal Financial Institutions Examination Council (FFIEC) BSA/AML Examination Manual. The FFIEC BSA/AML Working Group, which the FDIC chairs, collaborated with other federal banking agencies and the Financial Crimes Enforcement Network (FinCEN) on the revision project.



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### **Promoting Economic Inclusion**

The FDIC has long been committed to bringing all segments of society into the financial mainstream. This year, the Board approved the establishment of the FDIC Advisory Committee on Economic Inclusion to provide the FDIC with advice and recommendations on important initiatives focused on expanding access to banking services by underserved populations. The Committee members represent a broad cross section of interests from the banking industry, state regulatory authorities, government, academia, consumer and public advocacy organizations, community-based groups and others impacted by banking-related practices.

This year, the FDIC took two important steps to focus attention on the need for affordable small-dollar loan products. First, the FDIC released *Affordable Small-Dollar Loan Guidelines* for public comment. The guidelines explore several aspects of product development, including affordability, streamlined underwriting and savings. Second, the FDIC hosted a conference in December on meeting the needs of military personnel and their families, who are frequently turning to high-cost providers for short-term loans and other financial services. The banks that attended the conference developed a template for an affordable, small denomination loan product with a savings component. We will continue to work with the industry to find ways to promote both affordable short-term loan products and creative ways to encourage savings.

To reach an even wider audience of unbanked and underbanked with our successful *Money Smart* financial education program, this year the curriculum was released in Russian, large print and Braille. Release of the Braille and large-print versions was the first time that a financial education program has been specifically targeted for individuals with visual impairments. The FDIC also completed development of a Spanish-language version of our online Electronic Deposit Insurance Estimator and a Spanish-language video on federal deposit insurance coverage.

As part of our ongoing effort to help combat identity theft, we continued to take a leadership role in consumer education initiatives and released an online training tool called *Don't Be an Online Victim: How to Guard Against Internet Thieves and Electronic Scams*. The training tool is available through the FDIC's Web site and via disc.

In 2006, we continued to analyze the economies adversely affected by Gulf Coast hurricanes and worked closely with banks and consumers to address issues of concern. We also worked closely with other federal and state regulatory agencies to issue guidance outlining examination procedures for assessing the financial condition of institutions adversely affected by the hurricanes. The FDIC, working jointly with NeighborWorks® America, released a homeownership and financial counseling guide called *Navigating the Road to Housing Recovery in the Gulf Coast*. This guide was a focal point of an FDIC/NeighborWorks® Gulf Coast Housing Summit held in New Orleans in October that was attended by bankers, housing experts, homeownership counselors and others.

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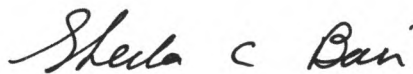
### **Conclusion**

Finally, I am pleased to note that we were able to enhance our efforts in each of our major business lines during 2006 while maintaining strong fiscal discipline. As detailed elsewhere in the report, the FDIC has had an extraordinary record of controlling its operating expenses over the past five years. Spending against the FDIC's operating budget in 2006 was 18 percent lower than it was in 2002, due primarily to a 27 percent reduction in the Corporation's staffing and limited resolution and receivership management activities during that period. These staff reductions completed more than a decade of downsizing that followed the Corporation's rapid workforce buildup to address the banking crisis of the late 1980s and early 1990s. I am indebted to my predecessor, Donald Powell, for his efforts to move the FDIC past the difficult era of downsizing, and for leaving me with a revitalized workforce that is eager and willing to address the new and emerging challenges to the safety and stability of our banking system.

Our agenda for 2007 will be full of challenges. Along with continuing to implement the changes brought about by deposit insurance reform, we will focus our energies on continuing to ensure the safety and soundness of our banking system, the effectiveness of our consumer protection efforts and the efficiency of our internal operations.

On a personal note, I would like to say that I am honored to serve as the 19th Chairman of the FDIC. Having been sworn in as Chairman on June 26, 2006, I clearly joined the FDIC at a critical – but exciting – time for the agency and the industry. I look forward to working alongside our outstanding Board and the dedicated employees of the FDIC as we face the challenges of the future together.

Sincerely,



**Sheila C. Bair**



Sheila C. Bair becomes FDIC Chairman as Executive Secretary Robert Feldman administers the oath and Deputy to the Chairman Alice Goodman holds the Bible.

## *Message from the Chief Financial Officer • Steven O. App*



I am pleased to join Chairman Bair in presenting our 2006 Annual Report. The report covers financial and program performance information and summarizes our successes for the year. The FDIC takes pride in providing timely, reliable and meaningful information to its many stakeholders.

As a result of the passage of deposit insurance reform legislation, the Bank Insurance Fund and the Savings Association Insurance Fund were merged on March 31, 2006, to create the Deposit Insurance Fund (DIF). Overall, the combined fund remained financially sound throughout the year and I can proudly report that the U.S. Government Accountability Office (GAO), for the fifteenth consecutive year, issued unqualified audit opinions on the annual financial statements for both funds administered by the FDIC – the DIF and the Federal Savings and Loan Insurance Corporation (FSLIC) Resolution Fund. These unqualified audit opinions validate our efforts to ensure that the financial statements of the funds for which we are stewards are fairly presented. This achievement also exemplifies the hard work and dedication of the FDIC staff.

FDIC's financial highlights during 2006 include:

In 2006, DIF's comprehensive income totaled \$1.6 billion compared to \$1.1 billion in 2005, a year-over-year increase of approximately 44 percent. Excluding the recognition of exit fees earned of \$345 million (a one-time adjustment), comprehensive income rose by \$133 million from a year ago. This year-over-year increase is primarily due to a decrease in the unrealized loss on available-for-sale (AFS) securities of \$348 million, which was offset by decreases in both interest earned on U.S. Treasury obligations of \$101 million and the negative provision for insurance losses of \$108 million.

The significantly lower unrealized loss on AFS securities primarily resulted from: 1) a smaller total market value of AFS securities, 2) a lower average duration for the AFS securities, and 3) a smaller increase in the market yields of the AFS securities. However, the lower unrealized loss was partially offset by a decrease in interest revenue on U.S. Treasury obligations that resulted from lower inflation compensation on Treasury Inflation-Protected Securities.

During 2006, we continued our efforts to control costs and to prudently manage the funds administered by the FDIC. Annual budgeted operating expenditures in 2006 totaled approximately \$973 million, which represents a decline of \$17 million (1.7 percent) from 2005. As Chairman Bair indicates in her message, the FDIC has an exceptional record of controlling its budgeted operational spending, which declined by \$216 million (18 percent) from 2002 to 2006. The FDIC Board of Directors, on December 5, 2006, approved a 2007 Corporate Operating Budget totaling \$1.1 billion, a modest 4.6 percent increase over the 2006 budget, largely due to the cost of employee pay increases negotiated for 2007.

Capital investment spending also declined substantially in 2006 to \$25 million. In 2006, we completed two major investment projects, the Virginia Square Phase II building and the New Financial Environment (NFE) (an integrated state-of-the-art financial system), reducing to three the inventory of active investment projects. This is down from a high of ten active projects in 2003 and 2004. In late 2006,

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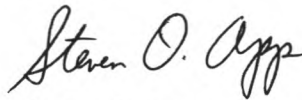
the FDIC Board approved a new investment project, an insurance claims determination system. It is the first new investment project approved since 2003. Investment spending is projected to total between \$19 million and \$23 million in 2007.

We are especially proud of our staff for the successful completion of Virginia Square Phase II – an outstanding facility that should serve the Corporation well for years to come. The project was completed on time and under budget, and has begun to yield substantial cost savings for the FDIC. We are also beginning to explore how to leverage the enhanced capabilities of the NFE to continue to improve our financial and cost management.

In accordance with the requirements of the Federal Managers' Financial Integrity Act of 1982, the FDIC's management conducted its annual assessment and concluded that the system of internal controls, taken as a whole, complies with internal control standards prescribed by the GAO and provides reasonable assurance that the related objectives are being met.

Looking ahead to 2007, the FDIC will continue to work toward sound management of the Corporation's financial and other resources.

Sincerely,



**Steven O. App**

## I. Management's Discussion and Analysis

### The Year in Review

During 2006, the FDIC faced many high-profile policy issues, ranging from deposit insurance reform, to capital reform, to the appropriate role of industrial loan companies. In addressing these issues the Corporation published numerous notices of proposed rulemaking throughout the year, seeking comment from the public and issued final rules to implement most of the components of deposit insurance reform legislation enacted early in the year. The Corporation also maintained its emphasis on a strong supervisory program, and pursued financial education and outreach initiatives focusing primarily on those adversely affected by Hurricanes Katrina and Rita and those not participating in the banking system. For the second year in a row, there were no insured institution failures, reflecting the continued strong health of the banking and thrift industry.

Highlighted in this section are the Corporation's 2006 accomplishments in each of its three major business lines – Insurance; Supervision and Consumer Protection; and Receivership Management – as well as its program support areas.

### Insurance

The FDIC insures bank and savings association deposits. As insurer, the FDIC must continually evaluate and effectively manage how changes in the economy, the financial markets and the banking system affect the adequacy and the viability of the deposit insurance fund.

#### Deposit Insurance Reform

In February 2006, the President signed into law the Federal Deposit Insurance Reform Act of 2005 and the Federal Deposit Insurance Reform Conforming Amendments Act of 2005. These new statutes instituted most of the key changes in the deposit insurance system that the FDIC had been pursuing for the previous five years. The Reform Act:

- Merges the Bank Insurance Fund (BIF) and the Savings Association Insurance Fund (SAIF) into the new Deposit Insurance Fund (DIF).
- Permits the FDIC's Board of Directors to price deposit insurance according to risk for all insured institutions, regardless of the level of the reserve ratio.
- Grants a one-time initial assessment credit of approximately \$4.7 billion to recognize institutions' past contributions to the combined fund.
- Establishes a range for the Designated Reserve Ratio (DRR) of 1.15 percent to 1.50 percent, and allows the FDIC to manage the reserve ratio within this range. Also requires that, if the reserve ratio falls below 1.15 percent or is expected to do so within six months, the FDIC must adopt a restoration plan that provides that the DIF will return the reserve ratio to 1.15 percent within five years.
- Generally mandates dividends to the industry of one-half of any amount above the 1.35 percent level and of all amounts in the fund above the 1.50 percent level.
- Increases the coverage limit for certain retirement accounts to \$250,000 but leaves the basic insurance limit for other deposits at \$100,000.
- Indexes both coverage limits for inflation, and allows the FDIC (in conjunction with the National Credit Union Administration) to increase the limits every five years beginning January 1, 2011, if warranted.



President George W. Bush in the Oval Office, signs the Federal Deposit Insurance Reform Act of 2005. Signing ceremony participants (l to r): Rep. Spencer Bachus, Sen. Tim Johnson, Sen. Paul Sarbanes, Sen. Richard Shelby, Rep. Mike Oxley, Rep. Darlene Hooley, Sen. Mike Enzi, and Martin Gruenberg, Vice Chairman – FDIC.

Implementation of deposit insurance reform was a major initiative for the FDIC in 2006. On March 14, 2006, the Board adopted an interim final rule implementing the substantive changes to the FDIC's insurance coverage rules, effective April 1, 2006. (A final rule was adopted on September 5, 2006.) In addition, the FDIC merged the BIF and SAIF into the newly-created DIF, effective March 31, 2006, prior to the statutory deadline effective date of July 1, 2006.

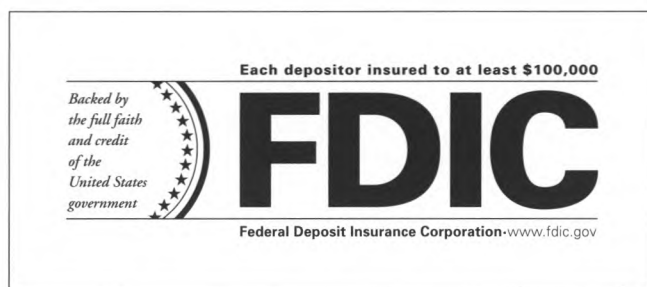
On October 10, 2006, after considering comments on a notice of proposed rulemaking (NPR) published in May 2006, the Board adopted a final rule governing the distribution and use of the \$4.7 billion one-time assessment credit. After considering comments on another NPR published in May 2006, the FDIC Board also adopted on October 10, 2006, a temporary final rule governing dividends from the DIF. Under this temporary rule, any dividend will be distributed based upon an institution's portion of the December 31, 1996, assessment base. In 2007, the FDIC will undertake a more comprehensive rulemaking on dividends to replace the temporary rule.

On November 2, 2006, after considering comments on an NPR published in July 2006, the Board adopted a final rule setting the DRR at 1.25 percent. The Board also adopted two final rules governing assessments after considering comments on NPRs published in May and July 2006. One of these rules makes operational changes to the assessment system. Under that rule, assessments will be determined and collected after the end of each quarter, which will permit consideration of more current supervisory information and capital data. Among its other provisions, the rule requires larger institutions to use average daily deposit balances as the basis for assessments.

The other rule establishes new assessment rates based on four new risk categories. Effective January 1, 2007, assessment rates will range from 5 to 7 basis points for Risk Category I institutions and will be 10 basis points for Risk Category II institutions, 28 basis points for Risk Category III institutions and 43 basis points for Risk Category IV institutions. Base assessment

rates range from 2 to 4 basis points for Risk Category I institutions and are 7 basis points for Risk Category II institutions, 25 basis points for Risk Category III institutions and 40 basis points for Risk Category IV institutions. The Board retains the flexibility to adjust rates in the future, within limits, without further notice-and-comment rulemaking.

In addition to the extensive rulemaking required in conjunction with the implementation of deposit insurance reform, fundamental changes were made in the FDIC's business functions including modification to major application systems such as the Risk-Related Premium System, Electronic Deposit Insurance Estimator, the Corporate Business Information System and the Assessment Information Management System. As part of the implementation, the FDIC also made available online new tools such as the One-Time Assessment Credit Search Tool and the Assessment Rate Calculator for insured institutions. System changes in support of deposit insurance reform will continue in 2007.



The new FDIC official teller sign reflects changes from deposit insurance reform.

### Risk-Related Premiums

The accompanying table shows the number and percentage of institutions insured by the Deposit Insurance Fund (DIF) as of September 30, 2006, according to risk classifications effective for the second semi-annual assessment period of 2006. Each institution is categorized based on its capital group (1, 2, or 3) and supervisory subgroup (A, B, or C), which is generally determined by on-site examinations. Assessment rates are basis points, cents per \$100 of assessable deposits, per year.

### Capital Standards

The FDIC, as insurer, has a substantial interest in ensuring that bank capital regulation effectively serves its function of safeguarding the federal bank safety net against excessive loss. During 2006, the FDIC participated on the Basel Committee on Banking Supervision and many of its sub-groups. The FDIC also participated in various U.S. regulatory efforts aimed at interpreting international standards and establishing sound policy and procedures for implementing these standards.

One of the FDIC's key objectives has been to ensure the adequacy of insured institutions' capital under Basel II. In 2006, the FDIC devoted substantial resources to domestic and international efforts to ensure that the new capital rules are designed and implemented appropriately. These efforts included the publication in September 2006 of an NPR seeking comment on draft rules for Basel II and revisions to the Market Risk Rule and the continued development of examination guidance, which is intended to provide the industry with regulatory perspectives on implementation.

### Risk-Related Premiums

Capital Group	Supervisory Risk Subgroup		
	A	B	C
<b>1. Well Capitalized:</b>			
Assessment Rate	0	3	17
Number of Institutions	8,324 (95.1%)	345 (4.0%)	38 (0.4%)
<b>2. Adequately Capitalized:</b>			
Assessment Rate	3	10	24
Number of Institutions	39 (0.5%)	3 (0.0%)	1 (0.0%)
<b>3. Undercapitalized:</b>			
Assessment Rate	10	24	27
Number of Institutions	2 (0.0%)	0 (0.0%)	3 (0.0%)

The findings of the fourth quantitative impact study (QIS-4), which were completed in 2005, suggested that, without modification, the Basel II framework could result in a significant decline in minimum risk-based capital requirements. As a result, several safeguards were incorporated into the Basel II NPR to protect against a significant decline in minimum risk-based capital requirements. These safeguards included a one-year delay in the targeted effective date of the regulation, a longer transition period, limitations on the amount that risk-based capital at individual banks could decline during the transition period, the retention of the U.S. leverage ratio and Prompt Corrective Action requirements, and a 10 percent downward limit on the aggregate reduction in minimum risk-based capital that could result from the implementation of Basel II. Through continuing on-site and off-site reviews of all FDIC-supervised institutions that have indicated possible plans to operate under the new Basel Capital Accord, the Corporation has confirmed that those institutions are making satisfactory progress towards meeting the expected requirements.

The FDIC is actively involved in efforts to revise the existing risk-based capital standards for those banks that will not be subject to Basel II. These efforts, referred to as Basel IA, are intended to modernize the risk-based capital rules for non-Basel II banks to ensure that the framework remains a relevant and reliable measure of the risks present in the banking system and to minimize potential competitive inequities that may arise between banks that adopt Basel II and those banks that remain under the existing capital rules. The revisions proposed in the Basel IA NPR are anticipated to be finalized by domestic bank and thrift regulatory authorities in 2007 for implementation in January 2008. The Basel IA NPR was published in the Federal Register for public comment in December 2006.

### Regulatory Burden Reduction

Pursuant to Section 2222 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), federal banking regulators are required to review existing regulations to identify and eliminate



those that are outdated, unnecessary or unduly burdensome on insured depository institutions. An interagency EGRPRA work group completed a comprehensive three-year review in 2006, analyzing the comments received on the last sets of regulations and publishing a summary of those comments. The interagency working group also prepared a report to Congress, which identified significant issues raised during the public comment period.

The Financial Services Regulatory Relief Act of 2006 was enacted into law in October 2006. This Act requires the SEC and FRB to jointly issue a rule to implement the exceptions to the definition of *broker* in accordance with section 3(a)(4)(F) of the Securities Exchange Act of 1934, permits the Federal Reserve to pay interest on balances kept at the Federal Reserve Banks, increases the Federal Reserve Board's flexibility in setting certain reserve requirements, reduces some redundant bank filing requirements and makes numerous changes designed to enhance banking agency efficiency and effectiveness. The new law also expands eligibility for inclusion in the 18-month safety and soundness examination cycle to insured institutions with CAMELS<sup>1</sup> "1" ratings with up to \$500 million in assets (an increase from the previous threshold of \$250 million). Congress subsequently enacted legislation expanding eligibility for the 18-month examination cycle to insured institutions with CAMELS "2" ratings up to \$500 million in assets.

### **Center for Financial Research**

The FDIC's Center for Financial Research (CFR) co-sponsored two research conferences during 2006. The 16th annual Derivatives Securities and Risk Management Conference, which the FDIC co-sponsored with Cornell University's Johnson Graduate School of Management and the University of Houston's Bauer College of Business, was held in April 2006. In addition, the CFR and the *Journal for Financial Services Research* (JFSR) sponsored their sixth annual research conference in September 2006. The conference attracted academics from U.S. and foreign universities, U.S. and foreign bank supervisors, congressional staff, consultants and bankers. As a part of the conference, the CFR sponsored a symposium entitled "U.S. Implementation of Basel II," at which academics and U.S. and foreign bank regulators presented 12 research papers analyzing the potential effects of the new capital standards.

In addition to these conferences, the CFR and Harvard University jointly sponsored a brainstorming symposium to advance research on consumer finance in October 2006. Individuals from academia, businesses, public policy, consumer advocacy and philanthropy groups discussed and proposed a research agenda in the field of consumer finance.

Thirteen CFR working papers were completed and published in 2006 on topics dealing with risk measurement, capital allocation, deposit insurance, community development or regulations related to these topics. The CFR Senior Fellows met in January 2006 to discuss ongoing CFR research on Basel II, deposit insurance reform, developments in the area of consumer finance and CFR activities for the coming year.

### **Central Data Repository**

The FDIC continued to leverage its investment in the Federal Financial Institutions Examination Council's (FFIEC) Central Data Repository (CDR). The CDR streamlines the collection, validation and publication of financial institutions' Call Report data. The CDR was used to successfully collect Call Report data from approximately 8,000 reporting institutions for each quarter of 2006. The FFIEC also began work during 2006 on enhancing the CDR to publish data to the public and produce bank performance reports, and an interagency team began work on modifications that will increase the flexibility of the CDR to process additional data series.

The FDIC also continued to lead in the promulgation of the CDR's underlying financial reporting standard, XBRL (eXtensible Business Reporting Language), to increase financial transparency. Early in 2006, the FDIC formed an XBRL Advisory Group to build upon the success of the CDR program. Leveraging the FDIC's demonstrated expertise and

<sup>1</sup> The CAMELS composite rating represents the adequacy of **C**apital, the quality of **A**ssets, the capability of **M**anagement, the quality and level of **E**arnings, the adequacy of **L**iquidity, and the **S**ensitivity to market risk, and ranges from "1" (strongest) to "5" (weakest).

leadership in the field, the group will expand the use of XBRL technologies and promote their use among other FDIC business partners. Internal and external collaboration Web sites were established to allow the exchange of information and to disseminate lessons learned.

### **Risk Analysis Center**

The Risk Analysis Center (RAC) was established in 2003 to provide information about current and emerging risk issues. It is staffed with employees on detail from each of the FDIC's three business lines. The RAC uses interdivisional teams to analyze selected risk areas and carry out special projects which culminate in presentations and reports regarding these risk issues. The activities of the RAC are guided by the National Risk Committee, which is chaired by the Chief Operating Officer. In 2006, major projects of the RAC focused on collateralized debt obligations, operational risk, and the housing sector/alternative mortgage products. The RAC also reported to the National Risk Committee on a variety of other topics, including economic conditions, industry risk exposure, credit underwriting practices, and consumer protection issues.

### **Other Risk Identification Activities**

During 2006, the FDIC continued to research and analyze trends in the banking sector, financial markets, and the overall economy to identify emerging risks to the banking industry and the DIF. The identified risks were highlighted throughout the year in presentations and written reports. The FDIC prepared summary analyses

semiannually on the condition of large insured financial institutions, mainly based on information provided by FDIC examiners and these institutions' primary federal regulators. Institution-specific concerns were directed to FDIC regional offices for appropriate action. Additionally, the FDIC continued to analyze the regional economies adversely affected by hurricanes Katrina and Rita throughout the year.

The FDIC published a variety of studies in quarterly *FDIC Outlook* issues and periodic *FYI* reports that addressed a range of current topics in the banking sector, financial markets and the economy. In addition, quarterly *FDIC State Profiles* were released for each state during 2006. The FDIC also published the *Quarterly Banking Profile*, which discusses current conditions, trends and changes in the performance of insured institutions, and *Supervisory Insights*, which discusses implementation of regulatory policy, shares best practices and communicates emerging issues in bank supervision.

Throughout the year, the FDIC conducted numerous outreach activities addressing economic and banking risk analysis. Presentations were made to financial institutions and related trade groups, bank directors' colleges, community groups, foreign visitors and other regulators. The FDIC also sponsored a roundtable discussion that addressed possible scenarios for the next recession.

## **Supervision and Consumer Protection**

Supervision and consumer protection are cornerstones of the FDIC's efforts to ensure the stability of and public confidence in the nation's financial system. The FDIC's supervision program promotes the safety and soundness of FDIC-supervised insured depository institutions, protects consumers' rights, and promotes community investment initiatives. In addition to carrying out its established examination program and other supervisory activities, the FDIC initiated in 2006 a substantial expansion of its programs to promote economic inclusion and confronted difficult policy issues regarding industrial loan companies.

### **Examination Program**

The FDIC's strong bank examination program is the core component of its supervisory program. At year-end 2006, the Corporation was the primary federal regulator for 5,237 FDIC-insured state-chartered institutions that are not members of the Federal Reserve System (generally referred to as "state nonmember" institutions). Through safety and soundness, consumer compliance and the Community Reinvestment Act (CRA), and various specialty examinations, the FDIC assesses their operating condition, management practices and policies, and compliance with applicable laws and regulations. The FDIC also educates bankers and consumers on matters of interest and addresses consumers' questions and concerns.

In 2006, the Corporation conducted 2,388 statutorily-required safety and soundness examinations, including a review of Bank Secrecy Act compliance, and all required follow-up examinations for FDIC-supervised problem institutions within prescribed time frames. The FDIC also conducted 1,959 CRA/Compliance examinations (777 joint compliance-CRA examinations, 1,177 compliance-only examinations,<sup>2</sup> and five CRA-only examinations) and 3,052 specialty examinations. All compliance/CRA examinations were also conducted within the time frames established by FDIC policy, including required follow-up examinations of problem institutions. The accompanying table compares the number of examinations conducted in 2004, 2005 and 2006 by type.

As of December 31, 2006, there were 51 insured institutions with total assets of \$8.5 billion designated as problem institutions for safety and soundness purposes (defined as those institutions having a composite CAMELS<sup>3</sup> rating of "4" or "5"), compared to the same number of problem institutions with total assets of \$6.6 billion on December 31, 2005. This constituted a 28.7 percent year-over-year increase in the total assets in problem institutions. During 2006, 38 institutions with aggregate assets of \$4.7 billion were removed from the list of problem financial institutions, while 38 institutions with aggregate assets of \$7.8 billion were added to the list of problem financial institutions. The FDIC is the primary federal regulator for 27 of the 51 problem institutions.

### FDIC Examinations 2004-2006

	2006	2005	2004
<b>Safety and Soundness:</b>			
State Nonmember Banks	2,184	2,198	2,276
Savings Banks	201	199	236
Savings Associations	2	1	0
National Banks	0	0	0
State Member Banks	1	1	3
Subtotal - Safety and Soundness Examinations	2,388	2,399	2,515
<b>CRA/Compliance Examinations:</b>			
Compliance - Community Reinvestment Act	777	815	1,459
Compliance - only	1,177	1,198	673
CRA - only	5	7	4
Subtotal CRA/Compliance Examinations	1,959	2,020	2,136
<b>Specialty Examinations:</b>			
Trust Departments	468	450	534
Data Processing Facilities	2,584	2,708	2,570
Subtotal-Specialty Examinations	3,052	3,158	3,104
<b>Total</b>	<b>7,399</b>	<b>7,577</b>	<b>7,755</b>

During 2006, the Corporation issued the following formal and informal corrective actions to address safety and soundness concerns: 29 Cease and Desist Orders; one Written Agreement; and 146 Memoranda of Understanding. Of these actions issued, eight Cease and Desist Orders, one Written Agreement and 21 Memoranda of Understanding were issued based on apparent violations of the Bank Secrecy Act.

As of December 31, 2006, four FDIC-supervised institutions were assigned a "4" rating for compliance; no institutions were assigned a "5" rating. All of the "4"-rated institutions were examined in 2006, and

Memoranda of Understanding are currently being finalized to address the FDIC's examination findings. In addition, the FDIC developed and began using new screening tools in 2006 to identify those FDIC-supervised institutions with mortgage lending disparities, based upon "higher rate" pricing information supplied by these institutions under the Home Mortgage Disclosure Act (HMDA), and to assess whether the disparities in loan pricing and denial rates resulted from discriminatory lending or reflected other factors, such as creditworthiness, underwriting or other non-discriminatory criteria.<sup>4</sup> Compliance examinations were scheduled for all of the institutions with identified lending disparities to determine

<sup>2</sup> Compliance-only examinations are conducted for most institutions at or near the mid-point between joint compliance-CRA examinations under the Community Reinvestment Act of 1977, as amended by the Gramm-Leach-Bliley Act of 1999. CRA examinations of financial institutions with aggregate assets of \$250 million or less are subject to a CRA examination no more than once every five years if they receive a CRA rating of "Outstanding" and no more than once every four years if they receive a CRA rating of "Satisfactory" on their most recent examination.

<sup>3</sup> The CAMELS composite rating represents the adequacy of Capital, the quality of Assets, the capability of Management, the quality and level of Earnings, the adequacy of Liquidity, and the Sensitivity to market risk, and ranges from "1" (strongest) to "5" (weakest).

<sup>4</sup> The Federal Reserve Board began requiring covered institutions to report "higher rate" pricing information in their HMDA reports in 2004.

whether those disparities were the result of discriminatory lending. Although those examinations indicated that the majority of the institutions were not engaging in discriminatory lending, a small number of institutions were referred to the U.S. Department of Justice for engaging in an apparent pattern and practice of discriminatory lending.

### **Large Complex Financial Institution Program**

The FDIC's Large Bank Program was established to address the unique challenges associated with supervising and insuring the deposits of large and complex institutions. A significant share of the assets and insured deposits of the banking industry are today held in a small number of large institutions. The Program ensures a consistent approach to large bank supervision and risk analysis on a national basis by compiling key data and performing analyses of large-bank operations for use by various FDIC divisions and offices and by providing specialists to support supervisory activities for large banks. In 2006, guidelines were developed to enhance the FDIC's risk-monitoring program for large banks with assets greater than \$50 billion. Monitoring and assessment activities also continued in 2006 to ensure internal and industry preparedness for the implementation of Basel II. Training on credit and operational risk was conducted for regional and interagency personnel, and numerous "supervisory working group" meetings were held with foreign regulatory authorities to address Basel II home-host and cross-border issues.



Sandra Thompson, John Bovenzi, and Douglas Jones at an ILC hearing.

### **Industrial Loan Companies**

In 2006, an application for deposit insurance filed by a very large retailer on behalf of a proposed Utah industrial loan company (ILC) generated significant public interest. In April, the FDIC held three days of public hearings on the application. Nearly 70 representatives of financial institutions, trade associations, advocacy groups, the retailer, and others made presentations at the hearing. In addition, the FDIC received written statements from 16 parties who did not request an opportunity to present during the hearings.

As a result of that interest as well as congressional interest and reviews by the GAO and OIG, the FDIC initiated a comprehensive policy review of ILCs. On July 28, 2006, the Board imposed a moratorium extending through January 31, 2007, on the acceptance, approval, or denial of deposit insurance applications and change in control notices submitted by, or on behalf of, any ILC. The purpose of the moratorium was to permit the Corporation to evaluate industry developments; the various issues, facts and arguments raised

regarding the ILC charter; whether there are emerging safety and soundness issues or policy issues involving ILCs or other risks to the insurance fund; and whether statutory, regulatory or policy changes should be made in the FDIC's oversight of ILCs in order to protect the Deposit Insurance Fund or important congressional objectives.

The FDIC believes that public participation provides valuable insight into the issues presented by the recent trends and changes in the ILC industry. Accordingly, in order to obtain the public's insights, the FDIC invited comments on the ILC industry during a 45-day period that ended on October 10, 2006. In its Request for Public Comment, the FDIC posed 12 questions that sought public input on various topics, including the current legal framework of ILCs as well as the possible benefits, risks and supervisory issues associated with ILCs. At year-end 2006, eight ILC-related applications for deposit insurance and two change in control notices were pending.

### **Promoting Economic Inclusion**

The FDIC pursued a number of new initiatives in 2006 to promote broader access to banking services by traditionally underserved populations and to ensure adequate consumer protection in the provision of these services.

### **Advisory Committee on Economic Inclusion**

On November 2, 2006, the FDIC announced the establishment of an Advisory Committee on Economic Inclusion. The Committee will provide the FDIC with advice and recommendations on important initiatives focused on expanding access to banking services by underserved populations. It will also explore ways to encourage the banking industry to adopt suitable products and marketing strategies to compete with alternative high-cost providers. The Committee members will represent a cross section of interests from the banking industry, state regulatory authorities, government, academia, consumer or public advocacy organizations, community-based groups and others impacted by banking-related practices.

### **Alliance for Economic Inclusion**

In 2006, the FDIC created the Alliance for Economic Inclusion (AEI), a broad-based coalition of banks, community organizations, foundations, educators, and local, state, and federal agencies in each of the FDIC's six regions. The goal of the AEI initiative is to work with financial institutions

and other partners to bring those currently unbanked and underserved into the financial mainstream. The AEI will focus on expanding banking services in all underserved markets, including low- and moderate-income neighborhoods, minority communities and rural areas.

### **Affordable Small-Dollar Loan Guidelines**

To help meet consumer demand for affordable small-dollar loans, the FDIC issued a draft of its *Affordable Small-Dollar Loan Guidelines*, targeted to the banking industry, for public comment on December 4, 2006. Many consumers with bank accounts turn to high-cost payday or other non-bank lenders because they are accessible and can quickly provide small loans to cover unforeseen circumstances. The draft guidelines suggest ways the banking industry can make affordable short-term loan products more accessible to these customers, helping to build long-term, profitable multiple-account relationships. The guidelines focus on product development and underwriting, and include information on tools such as consumer financial education and savings that may address longer term financial issues. The FDIC expects to finalize the guidelines in early 2007.

### **Military Bank Initiative**

In late 2006, the FDIC began working closely with the banking industry to explore ways to make affordable short-term loan products more accessible to military personnel who frequently turn to high-cost providers for their financial services needs and to encourage individual and household savings by these borrowers. The FDIC established contact with the Association of Military Banks of

America (AMBA) and more than 125 banks located near military bases. Many of these banks have indicated a willingness to work with the FDIC in developing and providing an affordable small-denomination loan product, possibly with a savings component.

The FDIC hosted a conference with these banks in December 2006 in Washington, DC, to provide information and share ideas on successful product and marketing strategies for consumers in the military. Approximately 60 banks and more than 150 other participants – including press, bankers, trade associations and representatives of the Department of Defense – attended the conference on "Affordable, Responsible Loans for the Military: Programs and Prototypes." The program was organized with the assistance of the AMBA and featured Congressman Barney Frank and Kelvin Boston, host of PBS' *Moneywise*. The main focus of the event was the discussion of loan products targeted to or that have features that would benefit military borrowers. Following a discussion of regulatory issues, the participants attended workshops aimed at developing an affordable loan template. The FDIC intends to distribute this template to FDIC-supervised institutions in 2007 for use as a possible prototype in developing their own affordable loan programs.

### **Nontraditional Mortgage Products**

In 2006, the FDIC became increasingly concerned with the expansion of nontraditional mortgage products and the potential risk posed by these products to the DIF. While these products, which are also referred to as “alternative” or “exotic” mortgage loans, have been available for many years, the number of institutions offering them has expanded rapidly in recent years. To address these concerns, the FDIC implemented certain enhancements to the supervisory oversight of nontraditional mortgage banking activities and, with the other financial institution regulatory agencies, developed and issued guidance to address the growing risks associated with these loan products. The agencies are concerned that some borrowers may not fully understand the risks of these products. The agencies are also concerned about the lack of principal amortization and the potential for negative amortization. Moreover, institutions are increasingly combining these loans with other features that may compound risk.

The guidance covers three primary areas: loan terms and underwriting standards, portfolio and risk management practices, and consumer protection issues. It focuses on qualification standards for borrowers, and portfolio management and communication with consumers and makes clear that the FDIC and the other regulatory agencies expect institutions to effectively assess and manage the risks posed by nontraditional mortgage products.



Erica Bovenzi and Sandra Thompson at a community bank forum in New Orleans.

The guidance recommends that promotional materials and other product descriptions provide consumers with full and balanced information about the costs, terms, features and risks – particularly payment shock and negative amortization – of non-traditional mortgage products. To help consumers shop wisely and decide whether such a product is right for them, the FDIC also published information about nontraditional mortgages in its quarterly *FDIC Consumer News* and joined the other regulatory agencies in publishing a consumer handbook on interest-only and payment-option mortgages.

### **Guidance on Concentrations in Commercial Real Estate Lending**

The federal banking regulatory agencies (agencies) recognized that financial institutions serve a vital role in their communities by supplying credit for business and real estate development. However, the agencies have observed that commercial real estate (CRE) concentrations have been rising over the past several years and may expose institutions

to earnings and capital volatility in the event of economic downturn. To address these concerns, the agencies published for comment the proposed interagency *Guidance on Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices (CRE Guidance)* on January 10, 2006. After carefully reviewing over 4,400 comment letters, the agencies issued the final *CRE Guidance* on December 12, 2006. The *CRE Guidance* reminded institutions that strong underwriting standards, portfolio management practices, and capital levels are important elements of a sound CRE lending program.

### **Hurricane Recovery Assistance**

Since the Gulf Coast hurricanes of 2005, the FDIC has worked with other federal and state regulatory agencies to address policy issues that arose due to the severity and



Vice Chairman Gruenberg at a Gulf Coast forum in New Orleans.

scale of those events. In 2006, the agencies issued examiner guidance that outlines examination procedures for assessing the financial condition of institutions adversely affected by the hurricanes. Working through the Federal Financial Institutions Examination Council (FFIEC), the agencies also published and distributed to insured financial institutions a booklet entitled *Lessons Learned from Hurricane Katrina: Preparing Your Institution for a Catastrophic Event*. This booklet compiles the experiences of bank officials in the aftermath of these hurricanes and offers insights to those who are responsible for devising and implementing an institution's disaster recovery and business continuity plans.

In October 2006, the FDIC and NeighborWorks® America jointly released a new homeownership and financial counseling guide called *Navigating the Road to Housing Recovery in the Gulf Coast*. The

guide is designed for evacuees who are now beginning to receive federal and state financial assistance to rebuild or relocate. It was a focal point of two conferences held in late 2006, the "Gulf Coast Housing Summit—Strategies for Redeveloping Communities and Rebuilding Lives," jointly sponsored by the FDIC and NeighborWorks® America in New Orleans, LA, and another housing conference sponsored by Back Bay Mission in Biloxi, MS. More than 400 bankers, housing experts, homeownership counselors and others attended the two conferences to discuss local issues, match development resources with needs, and learn more about the "just-in-time" counseling program.

The FDIC, in cooperation with NeighborWorks® and an array of local partners, will schedule train-the-trainer sessions through early 2007 to develop 300 potential homeownership counselors. Counselor trainees will be drawn from banks, churches, government agencies, employers, nonprofits and other groups working with hurricane evacuees. This comprehensive

counseling program will assist individuals to plan carefully and make informed decisions to avoid costly mistakes at this difficult time in their lives. The FDIC envisions that the counseling program will become a template for consumers to "navigate the road to housing recovery" in other areas of the country following major natural disasters or other catastrophic events.

### Minority Depository Institutions

The FDIC has long recognized the importance of minority depository institutions in promoting the economic viability of minority and underserved communities. As a reflection of the FDIC's commitment to minority depository institutions, the FDIC issued a "Policy Statement Regarding Minority Depository Institutions" on April 9, 2002. The policy statement implements an outreach program designed to preserve and encourage minority ownership of financial institutions.

Since the adoption of that policy statement, the FDIC has maintained contact with various minority depository institution trade associations; met periodically with the other federal banking regulators to discuss initiatives underway at the FDIC and identify opportunities for the federal banking agencies to work together to assist minority institutions; held regional outreach meetings and five Minority Bankers Roundtables; and extended offers to each FDIC-supervised minority depository institution to meet and discuss issues of interest.

In August 2006, the FDIC hosted the first "National Minority Depository Institution Conference" in Miami, FL,

with attendance from more than 100 bankers; representatives from the Office of the Comptroller of the Currency, the Federal Reserve and the Office of Thrift Supervision; and several private-sector and industry trade group representatives. The conference addressed topics of interest to the minority banking community, with particular emphasis on a shared commitment to expanding financial services available to minority and underserved communities; developing coalitions to improve minority community infrastructures by partnering with organizations such as NeighborWorks® America; and fostering a better understanding by the regulatory community of the unique challenges minority depository institutions face. A second national conference is planned for 2007.

During 2006, an FDIC task force also assisted three minority institutions headquartered in New Orleans, LA, and severely impacted by Hurricane Katrina in improving their liquidity by securing \$22 million in deposit pledges from Utah-based ILCs. The ILCs also provided \$123,000 in direct cash donations to assist these institutions in meeting the housing and other needs of their employees.

### **Homeland Security**

The FDIC has taken a leadership role in ensuring that the financial sector—a critical part of the infrastructure of the United States—is prepared for a financial emergency. As a member of the Financial and Banking Information Infrastructure Committee (FBIIC), the

FDIC has sponsored a series of outreach meetings titled “Protecting the Financial Sector: A Public and Private Partnership.” During 2006, these Homeland Security meetings were held in 22 cities across the United States. These meetings provided members of the financial sector with the opportunity to communicate with senior government officials, law enforcement personnel, emergency management personnel and private sector leaders about emergency preparedness. Homeland Security meetings are planned for 11 cities in 2007.

### **Bank Secrecy Act**

The FDIC chairs the FFIEC Bank Secrecy Act/Anti-Money Laundering (BSA/AML) Working Group. Under the auspices of the BSA/AML Working Group, the FDIC, the other federal banking agencies, and FinCEN updated the FFIEC BSA/AML Examination Manual in July 2006. The revised manual reflects the ongoing commitment of the federal banking agencies and FinCEN to provide current and consistent guidance on risk-based policies, procedures, and processes for banking organizations to comply with the BSA and safeguarding operations from money laundering and terrorist financing. Following the release of the manual, the FDIC coordinated and hosted four interagency conference calls for the banking industry and examination staff regarding changes to the manual. Over 1,500 examiners and 10,650 bankers and industry representatives participated in those outreach events. During 2006, the FDIC also participated in more than 145 additional industry outreach and regulatory training events nationwide relating to BSA/AML topics.

The FDIC continued in 2006 to play a critical role in the international fight against money laundering and terrorist financing. Its efforts included the following:

- With the other federal banking agencies, negotiated and signed an information-sharing memorandum of understanding (MOU) with the Office of Foreign Assets Control (OFAC) in April 2006.
- Conducted AML/Counter-Financing of Terrorism (CFT) training for 20 central bank representatives from Afghanistan, Iraq, Kenya, South Africa, and Yemen in September 2006.
- Provided guidance and resources for the international AML/CFT financial system assessments and training. The FDIC participated in reviews of South Africa’s existing AML policies and Paraguay draft AML legislation; provided technical assistance in Bosnia to evaluate AML controls and existing legislation; delivered a presentation at the Eurasian Group (Financial Action Task Force-style regional body) seminar in Russia; and provided guidance to the Russian central bank, financial intelligence unit, and legislature regarding amendments to Russia’s AML law.



- Continued to enhance the skills of its BSA/AML subject-matter experts, with 34 BSA/AML subject-matter experts attaining certification during 2006 under the Association of Certified Anti-Money Laundering Specialist certification program.
- Conducted AML examination training courses for representatives from the Albanian financial intelligence unit, the Indian financial intelligence unit, and Malaysian government officials.

### **Cyber Fraud and Financial Crimes**

The FDIC continued to take a leadership role in consumer education initiatives related to identity theft with a public education campaign that included sponsoring identity theft symposia focusing on e-commerce. The symposia, held in San Francisco, CA, Mesa, AZ, and Miami Beach, FL, brought together representatives from federal and state governments, industry, consumer and community organizations, and law enforcement to discuss issues related to identity theft and e-commerce.

Other major accomplishments during 2006 in combating identity theft included the following:

- Assisted financial institutions in identifying and shutting down approximately 900 “phishing” Web sites. The term “phishing”—as in fishing for confidential information—refers to a scam that encompasses fraudulently obtaining and using an individual’s personal or financial information.
- Issued 342 special alerts of reported cases of counterfeit or fraudulent bank checks.
- Released an online training tool entitled “Don’t Be an On-line Victim: How to Guard Against Internet Thieves and Electronic Scams” (available through the FDIC’s Web site and on CD-ROM).
- Participated in the President’s Identity Theft Task Force and five of its primary subgroups.

### **Office of International Affairs**

Increasing globalization and interdependence heighten the potential for financial and economic instability to transcend national geographic boundaries. The promotion of sound, stable banking systems abroad is a key ingredient for greater global prosperity and stability which, in turn, will benefit the U.S. financial system and the banking public. The FDIC created the Office of International Affairs in 2006 to coordinate the FDIC’s international activities with a focus on building strong relationships with foreign regulators and deposit insurers, other U.S. government entities and international organizations. The programs overseen by the office provide training, expert consultation, and technical assistance to foreign deposit insurers, bank supervisory authorities and other foreign government agencies to support the development and maintenance of effective deposit insurance programs and stable, sound banking systems worldwide.

### **Consumer Complaints and Inquiries**

The FDIC investigates consumer complaints about FDIC-supervised institutions and answers inquiries from the public about consumer protection laws and banking practices. In 2006, the FDIC received 9,652 written complaints, of which 3,442 were against state nonmember institutions. The Corporation responded to over 97 percent of these complaints within corporate timeliness standards. The FDIC also responded to 3,870 written and 4,188 telephone inquiries from consumers and members of the banking community about consumer protection issues.

In April 2006, the FDIC hosted the first Interagency Consumer Affairs Conference in Arlington, VA, with approximately 140 attendees, including representatives from the Federal Reserve Board, Office of Thrift Supervision, Office of the Comptroller of the Currency, National Credit Union Administration, and the Federal Trade Commission. Discussions included best practices for investigating and responding to consumer complaints, banking practices, and financial trends that have and will continue to challenge consumers in 2006 and beyond.

### **Deposit Insurance Education**

An important part of the FDIC’s role in insuring deposits and protecting the rights of depositors is its responsibility to ensure that bankers and consumers have access to accurate information about the FDIC’s deposit insurance rules. The FDIC has an extensive deposit insurance education program consisting of seminars for bankers, electronic tools for estimating deposit insurance coverage, and

written and electronic information targeting both bankers and consumers. The FDIC also responds directly to inquiries from bankers and the public about deposit insurance. During 2006, the FDIC responded to over 86,134, or 99 percent, of written and telephone inquiries from bankers and consumers about the FDIC's deposit insurance program and insurance coverage issues within the time frames established by policy. This was an increase of approximately 34 percent over the number of inquiries received in 2005, in large part due to the enactment of new coverage limits as part of deposit insurance reform.

Following enactment of deposit insurance reform legislation, the FDIC initiated a multi-pronged effort to inform the public and banking industry about the increase in coverage for retirement savings. As part of this effort, the FDIC updated its numerous publications and educational tools for consumers and bankers on FDIC insurance coverage, including updated editions of *Insuring Your Deposits*, the FDIC's basic deposit insurance brochure for consumers; *Your Insured Deposit*, the FDIC's comprehensive deposit insurance guide; and the Electronic Deposit Insurance Estimator (EDIE), the FDIC's user-friendly Internet application that helps bank customers calculate insurance coverage on their deposit accounts at FDIC-insured institutions. The FDIC also published other promotional materials, including a special edition of the *FDIC Consumer News* that included information on the new coverage limits, and worked with

the banking industry, national consumer organizations and the media to publicize the availability of this information. More than 8,200 bankers participated in a series of national teleconferences on the new coverage limits conducted by the FDIC during the summer of 2006. In addition, the FDIC used a variety of formats to conduct 28 seminars for financial institution employees and consumer organizations on changes to deposit insurance coverage rules that were effective on April 1, 2006.

In 2006, the FDIC also completed development of Spanish-language versions of two of its most popular educational resources for consumers and bankers, a Spanish language version of EDIE (available on the FDIC's Web site beginning in early 2007) and a 30-minute Spanish-language video for bank employees and customers (now available on the FDIC's Web site) that provides an overview of the FDIC's rules and requirements for deposit insurance coverage, with specific emphasis on the most common account ownership categories used by individuals and families.

The FDIC continued publication of its quarterly consumer newsletter, *FDIC Consumer News*, which covers a wide range of financial topics of interest to consumers. Three special age-based issues of *FDIC Consumer News* – for seniors, young adults and teens – were published during the year. The how-to financial guide for seniors won an Achievement in Consumer Education Award from the National Association of Consumer Agency Administrators. Current and past issues of *FDIC Consumer News* are available online at [www.fdic.gov/consumernews](http://www.fdic.gov/consumernews).

### **Financial Education and Community Development**

Five years ago, the FDIC—recognizing the need for enhanced financial education across the country—inaugurated its award-winning *Money Smart* curriculum, which is now available in seven languages as well as in a computer-based instruction version. In 2006, the FDIC introduced the Russian language, large print and Braille versions of *Money Smart*. The large print and Braille versions are the first financial education program specifically targeted for individuals with visual impairments. Since its inception, over 864,000 individuals (including approximately 207,000 in 2006) have participated in *Money Smart* classes and approximately 128,000 of these participants have subsequently established new banking relationships.

During 2006, the FDIC also undertook 370 community development, technical assistance and outreach activities. These activities were designed to promote: awareness of investment opportunities to financial institutions, access to capital within communities, knowledge-sharing among the public and private sector, and wealth building opportunities for families. Representatives throughout the financial industry and their stakeholders collaborated with FDIC on a broad range of initiatives structured to meet local and regional needs for financial products and services, credit, asset-building, affordable housing, small business and micro-enterprise development and financial education.

## Receivership Management

The FDIC has the unique mission of protecting depositors of insured banks and savings associations. No depositor has ever experienced a loss on the insured amount of their deposit in an FDIC-insured institution due to a failure. Once an institution is closed by its chartering authority – the state for state-chartered institutions, the Office of the Comptroller of the Currency (OCC) for national banks and the Office of Thrift Supervision (OTS) for federal savings associations – the FDIC is responsible for resolving that failed bank or savings association. The FDIC gathers data about the troubled institution, estimates the potential loss to the insurance fund from various resolution alternatives, solicits and evaluates bids from potential acquirers, and recommends the least-costly resolution method to the FDIC's Board of Directors.

### Resolving Financial Institution Failures

For the second consecutive calendar year, there was no failure of an insured depository institution in 2006, further extending the longest period in the history of the FDIC during which no insured institution failed – a record 31 months. The Corporation's remaining receivership management workload also continued to decline. The accompanying chart provides liquidation highlights and trends for the past three years.

## Liquidation Highlights 2004-2006

Dollars in billions (except where noted)

	2006*	2005*	2004
Total Resolved Banks	0	0	3
Assets of Resolved Banks	\$ 0.00	\$ 0.00	\$ 0.15
Total Resolved Savings Associations	0	0	1
Assets of Resolved Savings Associations	\$ 0.00	\$ 0.00	\$ 0.01
Net Collections from Assets in Liquidation*	\$ 0.17	\$ 0.37	\$ 0.38
Total Assets in Liquidation*	\$ 0.35	\$ 0.44	\$ 0.61
Total Dividends Paid*	\$ 0.17	\$ 0.44	\$ 0.38
Savings Over Cost of Liquidation*	\$ 0	\$ 0	\$ 11.6 million

\* No failures in 2005 and 2006.

■ Includes activity from thrifts resolved by the former Federal Savings and Loan Insurance Corporation and the Resolution Trust Corporation.

▼ Least Cost Test Savings.

### Large Bank Contingency Planning

The FDIC must ensure that it has the tools and strategies necessary to fulfill its missions as deposit insurer and receiver for all insured banks and thrifts. As the banking industry has become more concentrated and as larger insured institutions have grown significantly, the FDIC has undertaken a number of concrete steps to enhance its capabilities to manage the resolution of a large bank. Some of the initiatives involved in this ongoing process are contingency planning exercises, system and process improvements for determination of deposit insurance claims and management of failing bank assets, consultations with domestic and international regulators, improvements to the FDIC's supervisory program for larger banks, and the designation of internal and external expertise to focus on larger bank issues. The Claims Administration System (CAS), described in the following section, is one of these initiatives. This effort will continue and evolve as the challenges change in the future.

### Claims Modernization Project

The FDIC is taking advantage of the hiatus in resolution activity by modernizing the way it determines the insurance status of depositors in the event of failure by streamlining its business processes and modernizing the internal systems used to facilitate a deposit insurance determination through improved use of current technology. This includes development and implementation of a new insurance determination system called the Claims Administration System (CAS) to be implemented in 2008, which will provide an integrated solution that will meet the current and future deposit insurance determination needs of the FDIC. The new system will minimize the potential for FDIC losses, reduce any spillover effects that could lead to systemic risks, preserve franchise value, and produce deposit insurance results in a timely manner in order to quickly provide funds to claimants.

The Corporation is also seeking cooperation from the largest insured institutions to assist in the insurance determination process in the event of failure. During 2006, the FDIC reviewed 28 comment letters received in response to an advance notice of proposed rulemaking (ANPR) published in December 2005, requesting input on three options that could be applied to the largest 145 insured institutions. Based on this review, a new ANPR was published in December 2006, seeking comment on a new option and strategy for this purpose. The FDIC is currently awaiting comments on this revised proposal.

### **Receivership Management**

The FDIC, as receiver, manages failed banks and their subsidiaries with the goal of expeditiously winding up their affairs. The oversight and prompt termination of receiverships help to preserve value for the uninsured depositors and other creditors by reducing overhead and other holding costs. Once the assets of a failed institution have been sold and all impediments to termination have been resolved, the FDIC makes the final distribution of any proceeds and terminates the receivership estate. In 2006, the number of receiverships under management was reduced by 15.4 percent (from 65 to 55), while the book value of assets under management was reduced by 20.2 percent (from \$441 million to \$352 million). The ten receiverships terminated in 2006 were all terminated within 90 days of the resolution of all impediments.

### **Professional Liability Recoveries**

The FDIC works to identify potential claims against directors and officers, accountants, appraisers, attorneys and other professionals who may have contributed to the failure of an insured financial institution. Once a claim is deemed viable and cost-effective to pursue, the FDIC initiates legal action against the appropriate parties. The FDIC strives to make a decision to close or pursue 80 percent of all potential claims within 18 months of the failure date.<sup>5</sup>

During 2006, the FDIC recovered approximately \$36.2 million from these professional liability suits. In addition, as part of the sentencing process for those convicted of criminal wrongdoing against failed institutions, the court may order a defendant to pay restitution to the receivership. The FDIC, working in conjunction with the U.S. Department of Justice, collected approximately \$10.5 million in criminal restitution payments during the year. The FDIC's caseload at the end of 2006 included investigations, lawsuits and ongoing settlement collections involving 13 claims and 95 other active collection matters, down from 127 at the beginning of 2006. At the end of 2006, there were 814 pending restitution orders, down from 995. This includes orders won by the former Resolution Trust Corporation for which the FDIC assumed responsibility on January 1, 1996.

### **Protecting Insured Depositors**

Although the FDIC's focus in recent years has shifted from resolving large numbers of failed institutions to addressing existing and emerging risks in insured depository institutions, the FDIC continues to protect depositors and other stakeholders of those institutions that fail. The FDIC's ability to attract healthy institutions to assume deposits and purchase assets of failed banks and savings associations minimizes the disruption to customers and allows some assets to be returned to the private sector immediately. Assets remaining after resolution are liquidated by the FDIC in an orderly manner, and the proceeds are used to pay creditors, including depositors whose accounts exceeded the insured limit. During 2006, the FDIC paid dividends of 80.2 percent of the deposit amount exceeding the insured limit, which represents an increase of 2.3 percent from 2005.

### **Effective Management of Strategic Resources**

The FDIC recognizes that it must effectively manage its human, financial, and technological resources in order to successfully carry out its mission and meet the performance goals and targets set forth in its annual performance plan. The Corporation must align these strategic resources with its mission and goals and deploy them where they are most needed in order to enhance its operational effectiveness and minimize potential financial risks to the DIF. Major accomplishments in improving the Corporation's operational efficiency and effectiveness during 2006 are described on the following pages.

<sup>5</sup> This performance target did not apply in 2006, because no failures occurred during the 18-month period prior to the start of the year.

### **Human Capital Management**

The FDIC's employees are its most important resource. The intellectual capital supplied by FDIC employees is the single most important contributor to achieving the Corporation's mission of maintaining public confidence in our nation's financial system. As such, the FDIC strives to be the best employer within the financial regulatory community and pursues human capital programs and strategies that will enable it to attract, develop and retain a highly skilled, diverse, and results-oriented workforce.

The FDIC has a human capital framework that guides its human capital activities. Using this framework as a guide, the Corporation continues to develop and maintain a workforce that is highly functional and cross-trained in multiple disciplines and stands ready to redirect its attention and efforts in response to changes in the banking industry or changes in workload priorities.

During 2006, the FDIC completed the last of its currently-planned workforce restructuring activities. Through the strategic use of voluntary early retirement authority and voluntary separation incentive payments, most of the remaining restructuring was accomplished voluntarily. The Corporation also completed a very successful internal placement process that reassigned remaining surplus staff to vacancies in other FDIC organizations.

### **Corporate Employee Program**

Development and implementation of the new Corporate Employee Program (CEP) continued in 2006. The program emphasizes cross-training of employees at all levels to provide greater flexibility to be able to respond to changes in workload as well as unexpected external events. During the past year, the primary focus was on the implementation of a new recruiting strategy for entry-level employees and refinement of the first-year training program under which new employees are exposed to each of the Corporation's three major business lines. By the end of 2006, almost 200 employees had begun the three-year career internship and training program that is the core component of the CEP and will in the future constitute the primary source of new employees for the Corporation's business divisions.

### **Employee Learning and Growth**

The Corporation emphasizes continuous employee learning and growth. During 2006, the Corporation finalized plans for the 2007 implementation of the new Professional Learning Account program that will give employees a greater role in planning their career development and provide substantially increased funding for external training. The Corporation also began to increase its emphasis on industry-recognized professional certifications and completed pilot tests of two new internally-developed certificate programs covering Bank Secrecy Act/Anti-Money Laundering, and Resolutions and Receivership Claims. A career path for large complex bank specialists will be explored,

and training requirements for this specialty will be evaluated. As these and other programs are implemented, a database of FDIC employee skills will track and monitor the availability of specialized human capital resources.

Corporate University expanded its support of external certificate programs to provide staff the opportunity to build skills as well as earn professional credentials. The FDIC now pays exam fees and preparation class fees for eligible students pursuing the following external certificate programs:

- Certified Anti-Money Laundering Specialist (CAMS);
- Certified Fraud Examiner (CFE);
- Certified Information Systems Auditor<sup>®</sup> (CISA<sup>®</sup>);
- Certified Regulatory Compliance Manager (CRCM);
- Chartered Financial Analyst<sup>®</sup> (CFA<sup>®</sup>); and
- Financial Risk Manager<sup>®</sup> (FRM<sup>®</sup>).

### **Succession Management**

The FDIC will have the opportunity over the next decade to substantially reshape its workforce in conjunction with the projected retirements of a large number of employees from the "baby boom" generation. To proactively plan for and address these projected retirements, the FDIC developed two succession management programs in 2006: the Executive Talent Review and the Corporate Executive Development Program. These programs were designed to assess executive leadership strength, identify potential skill set shortages or gaps and then institute strategies for closing these gaps, including rigorous leadership

development programs. In late 2006, the FDIC's senior leadership conducted an initial "talent review" of all of its executive managers to determine where there may be gaps in the availability and skills of qualified successors for key executive positions. This process identified a number of "at risk" positions – those in which the incumbents were likely to leave in the near future with no or few obvious internal candidates available to replace them. In 2007, the Corporation will develop strategies to fill these potential succession gaps for positions with a high risk of loss in the near term. The talent review process will also be extended to assess potential succession in management gaps for supervisory and managerial positions as well as senior technical professionals.

#### ***Pay-for-Performance***

In January 2006, the FDIC began implementation of the new 2006-2009 Compensation Agreement that had been negotiated with its employee union during 2005. This included a revised pay-for-performance (PFP) system that provides for graduated base pay increases and potential lump sum bonuses based exclusively on assessments of total employee performance. The PFP system is entirely performance-based; only those employees who meet all of their performance standards are eligible for pay increases.

#### ***Employee Engagement***

The FDIC's human capital programs and strategies are continually evaluated to ensure that the FDIC remains an employer of choice and that all employees feel engaged and aligned with the Corporation's mission critical functions. To help assess workload

alignment and employee engagement, all FDIC employees were encouraged to participate in the 2006 Federal Human Capital Survey administered by the Office of Personnel Management. This survey provides relative measures of employee satisfaction and engagement on a number of dimensions. In 2007, the FDIC will analyze the results and implement action plans to address any potential issues that employees identify as inhibitors to strong employee engagement.

#### **Management of Financial Resources**

The FDIC's operational expenses are largely paid from the DIF, and the Corporation seeks to operate in a consistently efficient and cost effective manner in order to fulfill its fiduciary responsibilities. To that end, the Corporation engages annually in a rigorous planning and budgeting process that is designed to ensure that budgeted resources are properly aligned with projected workload and business priorities. In 2006, the FDIC continued to enhance the cost management information available to managers in conjunction with the implementation of the New Financial Environment, its new accounting system. In 2007, the FDIC will continue to explore how best to utilize this enhanced cost management data to promote good stewardship of the Corporation's resources.

#### **Managing Facility-Related Costs**

In the first quarter of 2006, the Corporation completed construction of its Virginia Square Phase II facility in Arlington, VA. The project was

completed on time and under budget. Approximately 800 employees in three leased facilities in Washington, DC, were relocated to the expanded facility in Arlington. Successful completion of this initiative to build and relocate staff to owned space will save the Corporation an estimated \$89 million (net present value) over 20 years, compared to the projected cost of extending the previous leasing agreements.

#### **Information Technology Management**

Information technology (IT) resources are one of the most valuable assets available to the FDIC in fulfilling its corporate mission. The FDIC operates a nationwide computing network and maintains approximately 270 application systems through which employees perform their duties.

#### ***IT Transformation***

For the past several years, the Corporation has been engaged in a major effort to transform and improve its IT program. In 2006, the IT program continued to evolve as it continued to implement key elements of its transformation plan:

- The organization fully adopted the Rational Unified Process® as its new system development life cycle methodology and customized it to meet the FDIC's unique IT project environment.
- The Division of Information Technology (DIT) adopted a new internal control framework based upon the international standard known as CobiT (Control Objectives for Information and Related Technology).

- DIT continued implementing a new sourcing strategy in which it partnered with the private sector and other federal agencies to provide IT support services using performance-based, results-driven contracts.

### **E-Exam Programs**

In 2006, the FDIC also implemented an e-Exam Policy, including related security procedures, for use in conducting examination activities at institutions utilizing an electronic exchange of documents/data with the FDIC. A significant component of the e-Exam Policy involves the flexibility to increase the amount of examination work conducted off-site. Factors considered in the decision to utilize this program include the type and extent of the information available, the institution's risk profile, and management's willingness to transfer examination documents electronically.

### **E-Government**

The FDIC continued to collect quality and timely information in 2006 with the use of *FDICconnect*, the secure Web site that facilitates electronic communication with FDIC-insured institutions. In 2006, over 400,000 transactions were completed by financial institutions using *FDICconnect*.

### **Central Data Repository**

The Federal Financial Institutions Examination Council (FFIEC), which includes the FDIC, won a 2006 award from *Government Computer News*

for outstanding and innovative use of IT in government for the successful launch of the new Central Data Repository (CDR) to collect Call Report data using XBRL (eXtensible Business Reporting Language). The CDR project was also awarded the Chief Information Officer's Top 100 award for its outstanding work using XBRL for financial reporting.

### **Enhanced Information Security Program**

The FDIC's information security program seeks to proactively assure the integrity, confidentiality and availability of corporate information requiring an ongoing commitment by employees throughout the organization. In 2006, the information security program continued its ongoing cycle for assessing risks, developing and implementing effective security procedures and monitoring the effectiveness of those procedures.

### **Corporate Privacy Program**

The FDIC continued to enhance its IT Privacy Program in 2006 with an emphasis on protecting personally identifiable information (PII) from unauthorized use, access, disclosure or sharing, and protecting associated information systems from unauthorized access, modification, disruption or destruction. Initiatives undertaken during the year included the following:

- Developing an overarching privacy directive.
- Developing a strategy for the protection of PII processed, stored, transmitted or accessed by FDIC contractors, and ensuring appropriate assessment of the security of data.

- Continuing the review and remediation of PII in FDIC application systems.
- Identifying all contracts that process or use PII or other sensitive information, ensuring that updated privacy and nondisclosure clauses are included.
- Continuing to participate in the Office of Management and Budget Privacy Work Group.

### **Emergency Preparedness Program**

During 2006, the FDIC continued work on its Emergency Preparedness Program, and made improvements to the Emergency Response Plan (ERP) and Business Continuity Plan (BCP). Completed initiatives included the development of a computer-based instruction module on emergency preparedness for all FDIC personnel to be activated in early 2007; expansion and improvement of FDIC alternate site facilities; expansion of FDIC emergency notification systems to all regional and area offices; revision of both the ERP and BCP; and participation in the Federal government's *Forward Challenge* simulation exercise. Other accomplishments included the conduct of additional classroom training on emergency preparedness for employees, contractors and floor marshals; shelter-in-place and evacuation drills; and tabletop exercises at all headquarters and regional office locations. Disaster recovery testing of FDIC's key information technology resources was also performed.

## II. Financial Highlights

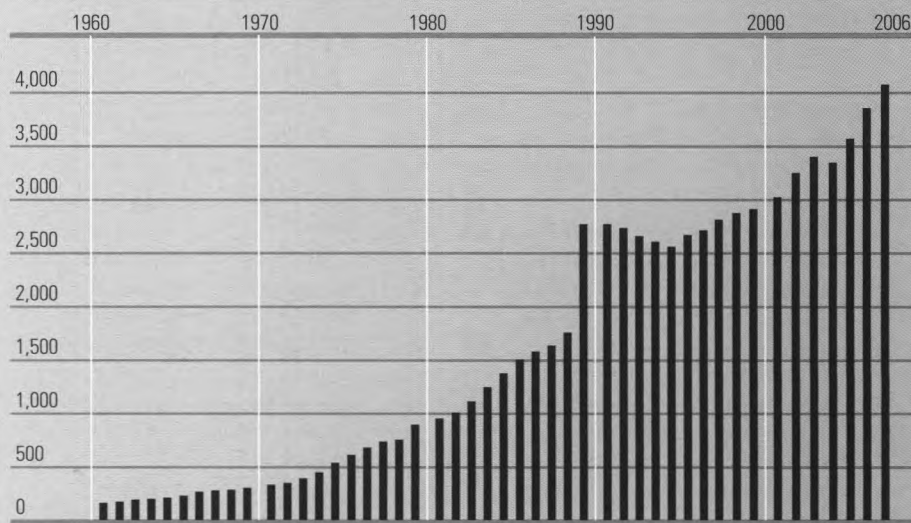
### Deposit Insurance Fund Performance

The FDIC administers the Deposit Insurance Fund (DIF) and the FSLIC Resolution Fund (FRF), which fulfills the obligations of the former Federal Savings and Loan Insurance Corporation (FSLIC) and the former Resolution Trust Corporation (RTC). The following summarizes the condition of the DIF. (See the accompanying tables on FDIC-DIF Insured Deposits on this page and DIF Insurance Fund Reserve Ratios on the following page.)

For the year 2006, DIF's comprehensive income totaled \$1.6 billion compared to \$1.1 billion in 2005, a year-over-year increase of approximately 44 percent. Excluding the recognition of exit fees earned of \$345 million (a one-time adjustment), comprehensive income rose by \$133 million from a year ago. This year-over-year increase is primarily due to a decrease in the unrealized loss on available-for-sale (AFS) securities of \$348 million, which was offset by decreases in both interest earned on U.S. Treasury obligations of \$101 million and the negative provision for loss of \$108 million. (See the accompanying chart on Selected Statistics on page 32.)

**FDIC-DIF Insured Deposits** (estimated 1960-2006)\*

Dollars in billions

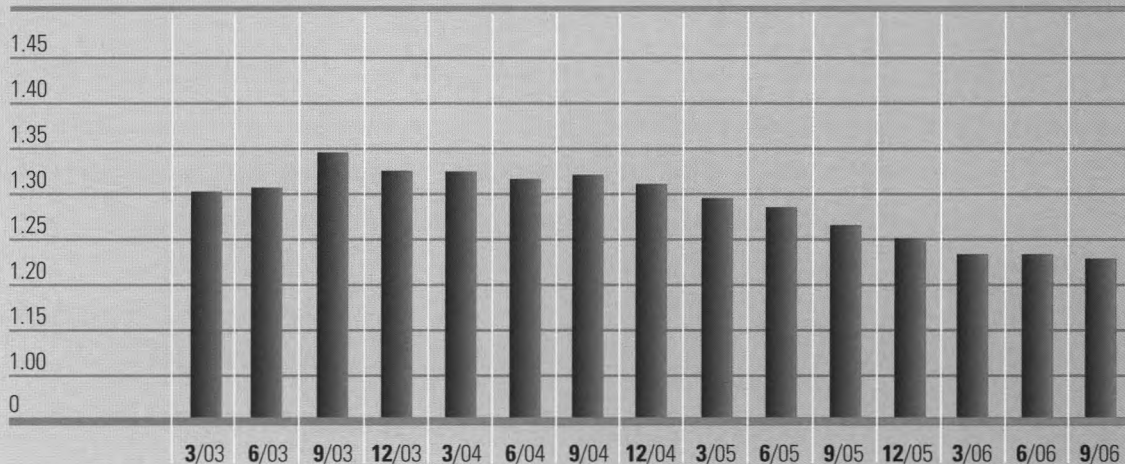


\* All amounts are year-end except 2006 is at 9/30/06.  
From 1989 through 2005, amounts represent the sum of separate BIF and SAIF amounts.  
Source: Commercial Bank Call Reports and Thrift Financial Reports.

The significantly lower unrealized loss on AFS securities primarily resulted from: 1) a smaller total market value of AFS securities, 2) a lower average duration for the AFS securities, and 3) a smaller increase in the market yields of the AFS securities. However, the lower unrealized loss was partially offset by a decrease in interest revenue on U.S. Treasury obligations that resulted from lower inflation compensation on Treasury Inflation-Protected Securities.



### DIF Insurance Fund Reserve Ratios (Fund Balances as a Percent of Insured Deposits)



Prior to 2006, amounts represent the sum of separate BIF and SAIF amounts.

## Selected Statistics Deposit Insurance Fund

Dollars in millions

For the years ended December 31

	2006	2005	2004
<b>Financial Results</b>			
Revenue	\$ 2,644	\$ 2,421	\$ 2,240
Operating Expenses	951	966	941
Insurance and other expenses	(46)	(156)	(334)
Net Income	1,739	1,611	1,633
Comprehensive Income	1,569	1,090	1,485
Insurance Fund Balance	\$ 50,165	\$ 48,597	\$ 47,507
Fund as a Percentage of Insured Deposits	1.22% <sup>▼</sup>	1.25%	1.31%
<b>Selected Statistics</b>			
Total DIF - Member Institutions <sup>•</sup>	8,743 <sup>▼</sup>	8,832	8,975
Problem Institutions	47 <sup>▼</sup>	52	80
Total Assets of Problem Institutions	\$ 3,983 <sup>▼</sup>	\$ 6,607	\$ 28,250
Institution Failures	0	0	4
Total Assets of Current Year Failed Institutions	\$ 0	\$ 0	\$ 166
Number of Active Failed Institution Receiverships	25	27	34

<sup>▼</sup> As of September 30, 2006.

<sup>•</sup> Commercial banks and savings institutions. Does not include U.S. branches of foreign banks.

## Corporate Operating Budget Spending

The FDIC has had an exceptional record of controlling operating costs over the past five years, and 2006 was no exception. Corporate Operating Budget expenses totaled \$973 million in 2006, including \$961 million for ongoing operations and \$12 million for receivership funding. During the five-year period from 2002 through 2006, the FDIC's annual Corporate Operating Budget expenses declined from \$1,189 million to \$973 million, a reduction of \$216 million, or 18 percent, despite

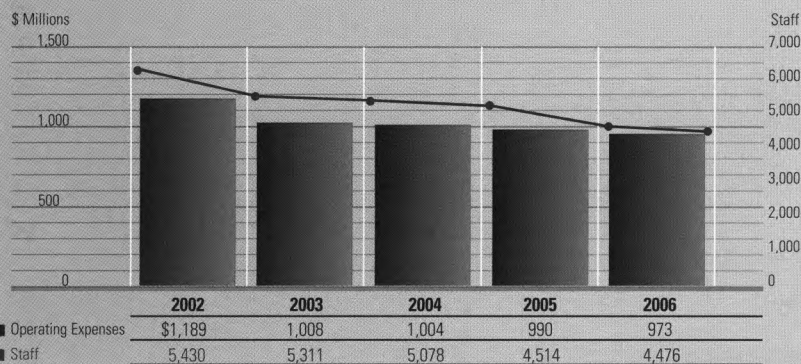
the effects of inflation on the FDIC's costs. That reduction was primarily attributable to significant reductions in staffing as well as a steady reduction in resolutions and receivership activities resulting from the historically low number of bank failures.

### Cost Reductions Realized through Staff Reductions

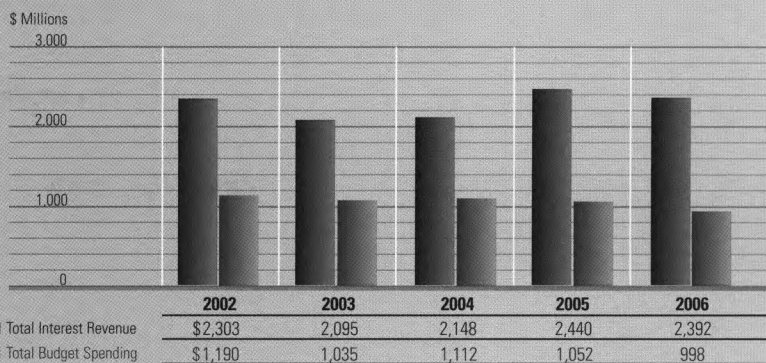
Salary and benefits costs represent more than 60 percent of the FDIC's annual Corporate Operating Budget. Because compensation costs are so significant, the FDIC has engaged in a continuing effort to realign staffing

to reflect reduced workload requirements as it has moved past the banking and thrift crisis. Total FDIC staffing fell from 6,167 at the beginning of 2002 to 4,476 at year-end 2006, a 27 percent reduction over five years. As a result, spending for salaries and benefits decreased by 15 percent, from \$737 million in 2002 to \$626 million in 2006, despite an increase of 17.7 percent in the salaries of individual employees during this period.

### FDIC Staffing and Operating Expenses



### Total Interest Revenue vs. Operating and Investment Budget Spending



#### A Continuing Record of Prudent Stewardship

Two comparisons illustrate the FDIC's prudent stewardship of the insurance and resolution funds over the past five years.

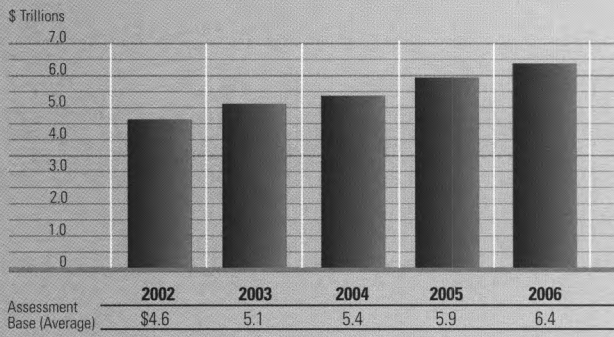
The FDIC relies primarily upon interest earned on the investments of the insurance and resolution funds for its operations. It is notable that the Corporation has reduced its operational spending even as the interest earned on the funds has increased

significantly. As a result, the FDIC's annual spending has dramatically declined as a percentage of interest revenue on the DIF and FRF. The aggregate interest revenue of the DIF and FRF grew to \$2,392 million in 2006, while combined operating and investment budget spending fell to 42 percent of interest revenue, down from 52 percent in 2002.

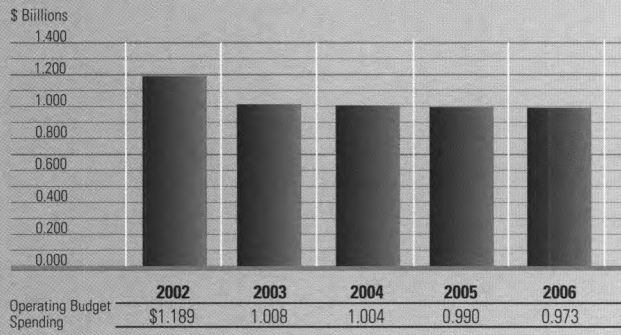
The Corporation's prudent stewardship of the funds can also be seen when operating budget spending is compared to the growth of the

industry over the past five years. The banking and thrift industry's deposit insurance assessment base rose by approximately 39 percent during this period, from \$4.6 trillion in 2002 to approximately \$6.4 trillion in 2006. During that same period, the FDIC's operating budget spending decreased by 18 percent. As a result, the FDIC's operating budget spending represented

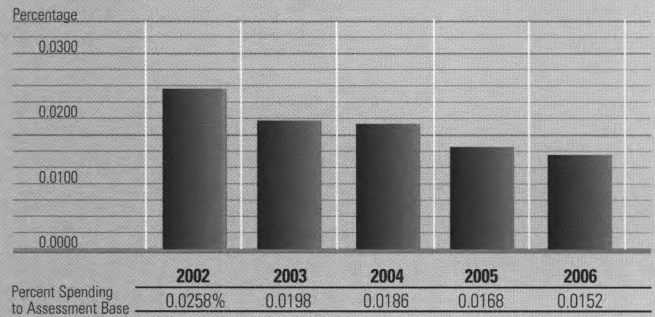
**As the Assessment Base Increased . . .**



**Operating Budget Spending Declined, and as a Result . . .**



**Spending has Declined Significantly as a Percentage of the Assessment Base.**



only 0.0152 percent of the average deposit insurance assessment base in 2006, compared to 0.0258 percent of the average deposit insurance assessment base in 2002.

These comparisons demonstrate the good value provided to the banking industry through the FDIC's continuing commitment to prudent stewardship of the DIF.

### **2007 Corporate Operating Budget**

Although its staffing realignment was essentially completed in 2006, the FDIC will continue to emphasize control of spending in 2007 and future years. In December 2006, the Board of Directors approved a 2007 Corporate Operating Budget of approximately \$1.107 billion, including \$1.032 billion for ongoing operations. The approved 2007 budget is 4.6 percent higher than the 2006 Corporate Operating Budget. This limited budget increase was required for negotiated employee pay increases and included funding for a number of major new initiatives, including additional staff for compliance examinations and other supervision functions, as well as

increased funding for employee training, enhanced IT security and privacy programs, and completion of system changes required to support the implementation of deposit insurance reform. The Corporation realigned its spending priorities and reduced costs in other areas to address these priority initiatives while limiting the size of the overall 2007 budget increase. In 2007 and future years, the FDIC will continue to rigorously review its workload and staffing and seek operational efficiencies through continuous improvement of its business processes.

### **Investment Spending**

The FDIC instituted a separate Investment Budget in 2003. It has a disciplined process for reviewing proposed new investment projects and managing the construction and implementation of approved projects. Most of the projects in the current investment portfolio are major IT system initiatives. Proposed IT projects are carefully reviewed to ensure that they are consistent with the Corporation's enterprise architecture. The project approval and monitoring processes also enable the FDIC to be aware of risks to the major capital investment projects and facilitate appropriate, timely intervention to address these risks throughout the development process. An investment portfolio performance review is provided to the FDIC's Board of Directors quarterly.

The Corporation undertook significant capital investments during the 2003-2006 period, including construction of a major expansion of its Virginia Square facility and the implementation of 11 major new IT systems. Investment spending totaled \$222 million during this period, peaking at \$108 million in 2004. Spending for investment projects in 2006 totaled approximately \$25 million. During 2006, the Corporation completed both the New Financial Environment (NFE) and Virginia Square Phase II investment projects.

In 2007, investment spending will total an estimated \$19 million to \$23 million. The Board of Directors approved one major new investment project for insurance determination, the Claims Administration System, in late 2006.

### *III. Performance Results Summary*

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#### **Summary of 2006 Performance Results by Program**

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The FDIC successfully achieved 27 of the 32 annual performance targets established in its 2006 Annual Performance Plan. Five performance targets related to the resolution of failed institutions were not applicable, because there were no insured institution failures in 2006. There were no instances in which 2006 performance had a material adverse effect on successful achievement of the FDIC's mission or its strategic goals and objectives regarding its major program responsibilities.

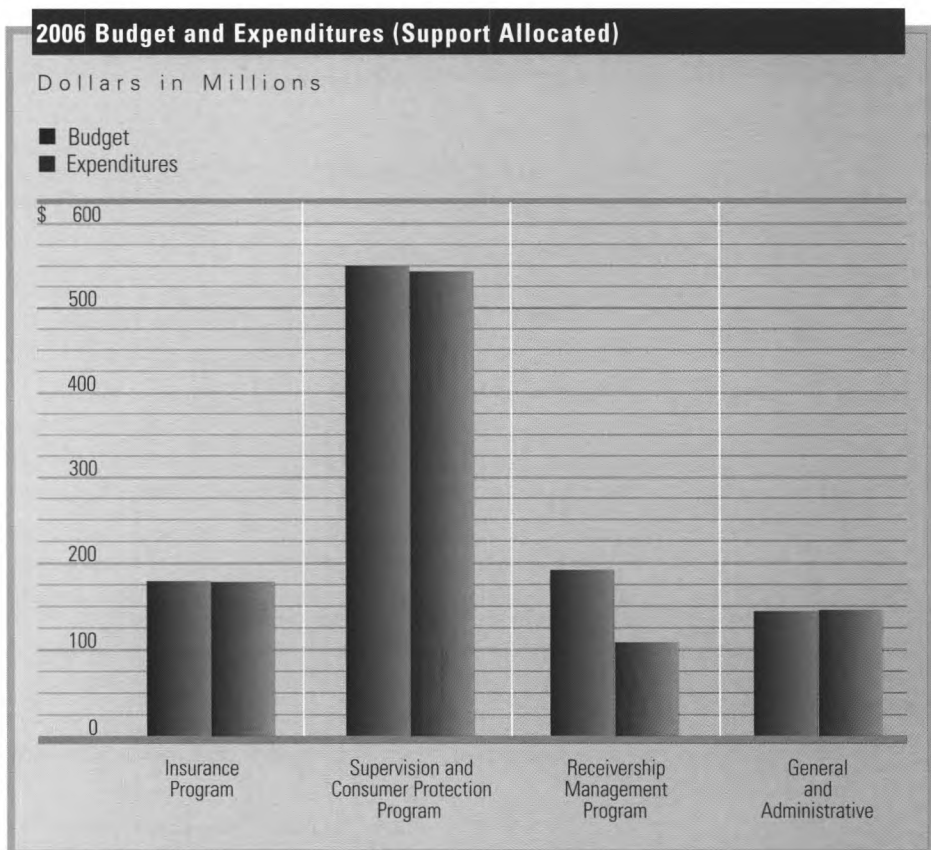
Key accomplishments by program are highlighted in the table on the following page.

Program Area	Performance Results
<b>Insurance</b>	<ul style="list-style-type: none"> <li>• Successfully implemented deposit insurance reform legislation.</li> <li>• Established new deposit insurance assessment rates, effective January 1, 2007, and a target Designated Reserve Ratio of 1.25, in accordance with the provisions of deposit insurance reform legislation.</li> <li>• Implemented new assessment credit and dividend systems, in accordance with the provisions of deposit insurance reform legislation.</li> <li>• Disseminated updated educational information and tools to consumers and bankers on changes in deposit insurance coverage limits.</li> <li>• Completed risk assessments for all large insured depository institutions and followed up on all identified concerns through off-site review and analysis.</li> <li>• Conducted and published analysis on the effects of Hurricanes Katrina and Rita.</li> <li>• Published numerous economic and banking information and analyses, through <i>FDIC Outlook</i>, <i>FYI</i> electronic bulletins, and Center for Financial Research Working Papers.</li> <li>• Completed reviews of the effectiveness of the reserving methodology.</li> <li>• No financial institution failures occurred during 2006.</li> </ul>
<b>Supervision and Consumer Protection</b>	<ul style="list-style-type: none"> <li>• Conducted 2,388 safety and soundness examinations, including required follow-up examinations of problem institutions, within prescribed time frames.</li> <li>• Conducted 1,959 compliance and Community Reinvestment Act examinations, including prescribed follow-up examination of problem institutions, within prescribed time frames.</li> <li>• Performed off-site reviews of 925 institutions.</li> <li>• Published Notices of Proposed Rulemaking for Basel II and IA, and continued other analytical and preparatory activities related to the implementation of these new capital regulations.</li> <li>• Completed advanced certification requirements for more than 10 percent of BSA/AML subject-matter experts.</li> <li>• Conducted 370 outreach and technical assistance events for bankers and community groups to promote awareness of community investment opportunities, access to capital, knowledge-sharing between the public and private sectors, and wealth building opportunities for families.</li> <li>• Continued to disseminate the award-winning <i>Money Smart</i> financial education curriculum in multiple languages, adding 157 <i>Money Smart</i> Alliance members; distributing an additional 121,768 copies of the curriculum; and training approximately 207,000 more individuals with the curriculum.</li> </ul>
<b>Receivership Management</b>	<ul style="list-style-type: none"> <li>• Terminated 10 of the 65 (15.4 percent) failed financial institution receiverships existing at the beginning of the year.</li> <li>• Secured approval for and began work on a new Claims Administration System (to be implemented in 2008).</li> <li>• No institution reached the 18-month milestone for professional liability claim investigation in 2006.</li> </ul>

## 2006 Budget and Expenditures by Program (Excluding Investments)

The FDIC budget for 2006 totaled \$1.050 billion. Excluding \$146 million for Corporate General and Administrative expenditures, budget amounts were allocated to corporate programs and related goals as follows: \$158 million, or 15 percent, to the Insurance program; \$557 million, or 53 percent, to the Supervision and Consumer Protection program; and \$189 million, or 18 percent, to the Receivership Management program.

Actual expenditures for the year totaled \$973 million. Excluding \$147 million for Corporate General and Administrative expenditures, actual expenditures were allocated to programs as follows: \$166 million, or 17 percent, to the Insurance program; \$548 million, or 56 percent, to the Supervision and Consumer Protection program; and \$112 million, or 12 percent, to the Receivership Management program.





## Performance Results by Program and Strategic Goal

### 2006 Insurance Program Results

#### Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.

Annual Performance Goal	Indicator	Target	Results
1. Respond promptly to all financial institution closings and emerging issues.	Number of business days after institution failure that depositors have access to insured funds either through transfer of deposits to successor insured depository institution or depositor payout.	If the failure occurs on a Friday, the target is one business day.  If a failure occurs on any other day of the week, the target is two business days.	Not Applicable. No failures in 2006. See pg. 25.  Not Applicable. No failures in 2006. See pg. 25.
	Enhancement of FDIC capabilities to make a deposit insurance determination for a large-bank failure.	Review comments received from the advance notice of proposed rulemaking on Large-Bank Deposit Insurance Determination Modernization, consult with stakeholders, and make a determination on how to proceed.	Achieved. See pgs. 25-26.
	2. Identify and address risks to the insurance funds.	Insurance risks posed by large insured depository institutions.	Assess the insurance risks in 100 percent of large insured depository institutions and adopt appropriate strategies.
Concerns referred for examination or other action.		Identify and follow up on 100 percent of issues raised through off-site review and analysis.	Achieved. See pg. 37.
3. Disseminate data and analyses on issues and risks affecting the financial services industry to bankers, supervisors, the public and other stakeholders.	Scope and timeliness of information dissemination on identified or potential issues and risks.	Results of research and analyses are disseminated in a timely manner through regular publications, ad hoc reports and other means.	Achieved. See pgs. 15-16.
		Industry outreach activities are undertaken to inform bankers and other stakeholders about current trends, concerns and other available FDIC resources.	Achieved. See pgs. 15-16, 19.

**2006 Insurance Program Results** (continued)

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
4. Maintain and improve the deposit insurance system.	Implementation of deposit insurance reform.	Develop and implement an assessment credit and dividends system and a new deposit insurance pricing system.	Achieved. See pg. 13.
		Implement deposit insurance reform legislation in accordance with statutorily prescribed time frames.	Achieved. See pgs. 12-13.
	Loss reserves.	Enhance the effectiveness of the reserving methodology by applying sophisticated analytical techniques to review variances between projected losses and actual losses, and by adjusting the methodology accordingly.	Achieved. See pg. 37.
	Fund adequacy.	Set assessment rates to maintain the insurance fund reserve ratio between 1.15 and 1.50 percent of estimated insured deposits.	Achieved. See pg. 13.

**2006 Insurance Program Results** (continued)

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
5. Provide educational information to insured depository institutions and their customers to help them understand the rules for determining the amount of insurance coverage on deposit accounts.	Utility of educational tools available to bankers and consumers.	Update <i>Insuring Your Deposits</i> (basic deposit insurance brochure for consumers), <i>Your Insured Deposit</i> (comprehensive deposit insurance brochure), and EDIE (Electronic Deposit Insurance Estimator) on the FDIC Web site to reflect changes resulting from enactment of deposit insurance reform legislation.	Achieved. See pg. 24.
		Develop and make available to the public an updated Spanish language version of EDIE reflecting deposit insurance reform.	Achieved. See pg. 24.
		Develop and make available to the public a Spanish language version of the FDIC's 30-minute video on deposit insurance coverage.	Achieved. See pg. 24.
		Respond to 90 percent of inquiries from consumers and bankers about FDIC deposit insurance coverage within time frames established by policy.	Achieved. See pg. 23.
		Respond to 90 percent of written inquiries within time frames established by policy.	Achieved. See pg. 23.

## 2006 Supervision and Consumer Protection Program Results

### Strategic Goal: FDIC-supervised institutions are safe and sound.

Annual Performance Goal	Indicator	Target	Results
1. Conduct on-site risk management examinations to assess the overall financial condition, management practices and policies, and compliance with applicable laws and regulations of FDIC-supervised depository institutions.	Percentage of required examinations conducted in accordance with statutory requirements and FDIC policy.	One hundred percent of required risk management examinations (including a review for Bank Secrecy Act (BSA) compliance) are conducted on schedule.	Achieved. See pg. 17.
2. Take prompt and effective supervisory action to address issues identified during the FDIC examination of FDIC-supervised institutions that receive a composite Uniform Financial Institutions Rating of "4" or "5" (problem institutions.) Monitor FDIC-supervised insured depository institutions' compliance with formal and informal enforcement actions.	Percentage of follow-up examinations of problem institutions conducted within required time frames.	One hundred percent of follow-up examinations are conducted within 12 months of completion of the prior examination.	Achieved. See pg. 17.
3. Increase regulatory knowledge to keep abreast of current issues related to money laundering and terrorist financing.	Certification of BSA/AML subject-matter experts.	At least 10 percent of BSA/AML subject-matter experts nationwide are certified under the Association of Certified Anti-Money Laundering Specialists certification program.	Achieved. See pg. 23.
4. More closely align regulatory capital with risk in large or multinational banks.	Continuation of preparatory activities related to the implementation of the new Basel Capital Accord (Basel II).	Publish a Notice of Proposed Rulemaking (NPR).  Participate in the continuing analysis of the projected results of the new capital regime.	Achieved. See pg. 14.  Achieved. See pg. 14.
5. More closely align regulatory capital with risk in banks not subject to Basel II capital rules.	Development of a revised capital framework proposal for institutions not subject to Basel II.	Develop a Notice of Proposed Rulemaking (NPR) for public issuance.	Achieved. See pg. 14.
6. Ensure that FDIC-supervised institutions that plan to operate under the new Basel Capital Accord are making satisfactory progress toward meeting required qualification standards.	Percentage of on-site examinations or off-site analyses performed.	On-site examinations or off-site analyses are performed for all FDIC-supervised banks that intend to operate under Basel II to ensure that they are effectively working toward meeting required qualification standards.	Achieved. See pg. 14.

**2006 Supervision and Consumer Protection Program Results** (continued)

**Strategic Goal: Consumers' rights are protected and FDIC-supervised institutions invest in their communities.**

Annual Performance Goal	Indicator	Target	Results
7. Conduct CRA and compliance examinations in accordance with the FDIC's examination frequency policy.	Percentage of examinations conducted in accordance with required time frames.	One hundred percent of required examinations are conducted within time frames established by FDIC policy.	Achieved. See pg. 17.
8. Take prompt and effective supervisory action to monitor and address problems identified during compliance examinations of FDIC-supervised institutions that receive a "4" or "5" rating for compliance with consumer protection and fair lending laws.	Percentage of follow-up examinations or related activities conducted within required time frames.	One hundred percent of follow-up examinations or related activities are conducted within 12 months from the date of a formal enforcement action to confirm that the institution is in compliance with the enforcement action.	Achieved. See pg. 17.
9. Provide effective outreach and technical assistance on topics related to the CRA, fair lending, and community development.	<p>Number of individuals taking a <i>Money Smart</i> class or using the self-paced curriculum.</p> <p>Number of outreach activities conducted, including technical assistance activities.</p>	<p>200,000 additional individuals are taught using the <i>Money Smart</i> curriculum.</p> <p>125 technical assistance (examination support) efforts or banker/community outreach activities are conducted related to CRA, fair lending, or community development.</p>	<p>Achieved. See pg. 24.</p> <p>Achieved. See pg. 24.</p>
10. Effectively meet the statutory mandate to investigate and respond to consumer complaints about FDIC-supervised financial institutions.	Timely responses to written complaints.	Responses are provided to 90 percent of written complaints within time frame established by policy.	Achieved. See pg. 23.

## 2006 Receivership Management Program Results

**Strategic Goal: Recovery to creditors of receivership is achieved.**

Annual Performance Goal	Indicator	Target	Results
1. Market failing institutions to all known qualified and interested potential bidders.	List of qualified and interested bidders.	Contact all known qualified and interested bidders.	Not Applicable. No failures in 2006. See pg. 25.
2. Value, manage, and market assets of failed institutions and their subsidiaries in a timely manner to maximize net return.	Percentage of failed institution's assets marketed.	Ninety percent of the book value of a failed institution's marketable assets are marketed within 90 days of failure.	Not Applicable. No failures in 2006. See pg. 26.
3. Manage the receivership estate and its subsidiaries toward an orderly termination.	Timely termination of new receiverships.	Terminate all receiverships within 90 days of the resolution of all impediments.	Achieved. See pg. 26.
4. Conduct investigations into all potential professional liability claim areas in all failed insured depository institutions and decide as promptly as possible to close or pursue each claim, considering the size and complexity of the institution.	Percentage of investigated claim areas for which a decision has been made to close or pursue the claim.	For 80 percent of all claim areas, a decision is made to close or pursue claims within 18 months of the failure date.	Not Applicable. No failures in 2006. See pg. 26.

## Prior Years Performance Results

(excerpted from the 2005 Annual Report) Page numbers refer to the 2005 report

### 2005 Insurance Program Results

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
1. Respond promptly to all financial institution closings and emerging issues.	Number of business days after institution failure by which depositors will have access to insured funds either through transfer of deposits to successor insured depository institution or depositor payout.	If the failure occurs on a Friday the target is one business day.  If the failure occurs on any other day of the week, the target is two business days.	Not Applicable. No failures in 2005.  Not Applicable. No failures in 2005.
2. Identify and address risks to the insurance funds.	Insurance risks posed by large insured depository institutions.	Assess the insurance risks in 100 percent of large insured depository institutions and adopt appropriate strategies.	Achieved. See pg. 29.
	Concerns referred for examination or other action.	Identify and follow up on 100 percent of referrals.	Achieved. See pg. 29.
	Dissemination of data and analyses on issues and risks affecting the banking industry to bankers, supervisors, the public, and other stakeholders.	Results of research and analyses are disseminated in a timely manner through regular publications, ad hoc reports and other means.	Achieved. See pg. 29.
		Industry outreach activities are undertaken to inform bankers and other stakeholders about current trends and concerns and available FDIC resources.	Achieved. See pgs. 10-11.
3. Maintain sufficient and reliable information on insured depository institutions.	Quality and timeliness of bank data.	Implement a modernized Call Reporting process during the second Call Reporting period in 2005.	Not Achieved. See pg. 11.
4. Maintain and improve the deposit insurance system.	Deposit Insurance Reform.	Provide information and analysis to Congressional committees in support of deposit insurance reform legislation.	Achieved. See pgs. 8-9.
		Obtain legislative support for a proposed assessment credit and rebate system and a new deposit insurance pricing system.	Achieved. See pgs. 8-9.

**2005 Insurance Program Results** (continued)

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
4. Maintain and improve the deposit insurance system. (continued)		When deposit insurance reform is enacted, implement legislation in accordance with statutorily prescribed time frames.	Not Applicable. Legislation enacted Feb. 8, 2006.
	Loss Reserves.	Enhance the effectiveness of the reserving methodology by applying sophisticated analytical techniques to review variances between projected losses and actual losses, and by adjusting the methodology accordingly.	Achieved. See pg. 29.
	Fund adequacy.	Set assessment rates to maintain the insurance funds at the designated reserve ratio (DRR), or return them to the DRR if they fall below it, as required by statute.	Achieved. See pg. 37.
		When deposit insurance reform legislation is enacted, promulgate rules and regulations establishing criteria for replenishing the Deposit Insurance Fund when it falls below the low end of the range.	Not Applicable. Legislation enacted Feb. 8, 2006.
5. Provide educational information to insured depository institutions and their customers to help them understand the rules for determining the amount of insurance coverage on deposit accounts.	Utility of educational tools developed for bankers and consumers.	Update the consumer version of the EDIE (Electronic Deposit Insurance Estimator) located on the FDIC's Web site.	Achieved. See pg. 18.



## 2005 Supervision and Consumer Protection Program Results

### Strategic Goal: FDIC-supervised institutions are safe and sound.

Annual Performance Goal	Indicator	Target	Results
1. Conduct on-site risk management examinations to assess an FDIC-supervised insured depository institution's overall financial condition, management practices and policies, and compliance with applicable laws and regulations.	Percentage of required examinations conducted in accordance with statutory requirements and FDIC policy.	One hundred percent of required safety and soundness examinations (including a review for BSA compliance) are conducted on schedule.	Achieved. See pg. 13.
2. Take prompt and effective supervisory actions to address problems found during the FDIC examination of FDIC-supervised institutions that receive a composite Uniform Financial Institutions Rating of "4" or "5" (problem institutions). Monitor FDIC-supervised insured depository institutions' compliance with formal and informal enforcement actions.	Percentage of follow-up examinations conducted within required time frames.	One hundred percent of follow-up examinations are conducted within 12 months of completion of the prior examination.	Achieved. See pg. 13.
3. Increase industry and regulatory awareness of emerging/high-risk areas.	Number of trained BSA/AML subject-matter experts.	The number of trained BSA/AML subject-matter experts increased to 300.	Achieved. See pg. 15.
	Number of industry outreach sessions on BSA/AML/Counter Financing of Terrorism (CFT) issues.	Advanced training is completed for all BSA/AML subject-matter experts.  At least one outreach session per region.	Achieved. See pg. 39.  Achieved. See pg. 15.
4. More closely align regulatory capital with risk in large or multinational banks.	Completion of preparatory activities for implementation of the new Basel Capital Accord.	Notice of Proposed Rule-making (NPR) and associated examination guidance for implementing the new Basel Capital Accord are published for comment.	Achieved. See pg. 10.
		Quantitative Impact Study 4 is completed.	Achieved. See pg. 9.

**2005 Supervision and Consumer Protection Program Results** (continued)

**Strategic Goal: FDIC-supervised institutions are safe and sound.**

Annual Performance Goal	Indicator	Target	Results
5. Ensure that FDIC-supervised institutions that plan to operate under the new Basel Capital Accord are making satisfactory progress toward meeting required qualification standards.	Percentage of on-site examinations or off-site analyses performed.	On-site examinations or off-site analyses are performed for all FDIC-supervised banks that intend to operate under Basel II to ensure that they are effectively working toward meeting required qualification standards.	Achieved. See pg. 9.
6. Provide effective outreach and technical assistance on topics related to the CRA, fair lending, and community development.	Number of <i>Money Smart</i> Alliance members.	200 additional members are added to the <i>Money Smart</i> Alliance.	Achieved. See pg. 38.
	Number of <i>Money Smart</i> curricula distributed.	20,000 additional copies of the <i>Money Smart</i> curricula are distributed.	Achieved. See pg. 38.
	Number of outreach activities conducted with technical assistance.	200,000 additional individuals are taught using the <i>Money Smart</i> curricula.  125 technical assistance (examination support) efforts or banker/community outreach activities are conducted related to CRA, fair lending, or community development.	Achieved. See pg. 38.  Achieved. See pg. 38.
7. Effectively meet the statutory mandate to investigate and respond to consumer complaints about FDIC-supervised financial institutions.	Timely responses to written complaints.	Responses are provided to 90 percent of written complaints within time frames established by policy.	Achieved. See pg. 17.
8. Conduct CRA and compliance examinations in accordance with the FDIC's examination frequency policy.	Percentage of examinations conducted within required time frames.	One hundred percent of required examinations are conducted within time frames established by FDIC policy.	Achieved. See pg. 13.
9. Take prompt and effective supervisory action to monitor and address problems identified during compliance examinations of FDIC-supervised institutions that receive a "4" or "5" rating for compliance with consumer protection and fair lending laws.	Percentage of follow-up examinations or related activities conducted within required time frames.	One hundred percent of follow-up examinations or related activities are conducted within 12 months from the date of a formal enforcement action to confirm that the institution is in compliance with the enforcement action.	Achieved. See pg. 39.

## 2005 Receivership Management Program Results

**Strategic Goal: Recovery to creditors of receiverships is achieved.**

Annual Performance Goal	Indicator	Target	Results
1. Market failing institutions to all known qualified and interested potential bidders.	List of qualified and interested bidders.	Contact all known qualified and interested bidders.	Not Applicable. No failures in 2005.
2. Value, manage, and market assets of failed institutions and their subsidiaries in a timely manner to maximize net return.	Percentage of failed institution's assets marketed.	Ninety percent of book value of a failed institution's marketable assets are marketed within 90 days of failure.	Not Applicable. No failures in 2005.
3. Manage the receivership estate and its subsidiaries toward an orderly termination.	Timely termination of new receiverships.	Inactivate 75 percent of receiverships managed through the Receivership Oversight Program within three years of the failure date.	Not Achieved. See pg. 40.
4. Conduct investigations into all potential professional liability claim areas in all failed insured depository institutions and decide as promptly as possible to close or pursue each claim, considering the size and complexity of the institution.	Percentage of investigated claim areas for which a decision has been made to close or pursue the claim.	For 80 percent of all claim areas, a decision is made to close or pursue the claim within 18 months after the failure date.	Achieved. See pg. 40.

## Prior Years Performance Results

(excerpted from the 2004 Annual Report) Page numbers refer to the 2004 report

### 2004 Insurance Program Results

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
1. Respond promptly to all financial institution closings and emerging issues.	Number of business days after institution failure by which depositors will have access to insured funds either through transfer of deposits to successor insured depository institution or depositor payout.	If the failure occurs on a Friday the target is one business day.  If the failure occurs on any other day of the week, the target is two business days.	Achieved. See pg. 19.  Not Applicable. All failures occurred on a Friday.
	2. Identify and address risks to the insurance funds.	Assess risks posed by large insured depository institutions.	Assess risks in 100 percent of large insured depository institutions and adopt appropriate strategies.
Identify and follow up on concerns referred for examination or other action (i.e., contact the insured institution or primary supervisor).		Identify and follow up on 100 percent of referrals.	Achieved. See pg. 12.
Disseminate data and analyses on current issues and risks affecting the banking industry to bankers, supervisors, stakeholders, and the public.		Analyses are included in regular publications or as ad hoc reports on a timely basis.	Achieved. See pg. 11.
		Conduct industry outreach activities aimed at the banking community and industry trade groups to discuss current trends and concerns and to inform bankers about available FDIC resources.	Achieved. See pg. 11.
3. Maintain sufficient and reliable information on insured depository institutions.	Maintain quality and timeliness of bank data.	Implement a modernized Call Reporting process by December 31, 2004.	Not Achieved. See pg. 11.

**2004 Insurance Program Results** (continued)

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
4. Maintain and improve the deposit insurance system.	Pursuit of changes to the deposit insurance system is in accordance with proposals submitted to the Congress.	Provide information and analysis to Congressional committees in support of deposit insurance reform legislation.	Achieved. See pgs. 8-9.
		Develop and obtain the necessary support for a proposed assessment credit and rebate system and a new deposit insurance pricing system.	Achieved. See pgs. 8-9.
		When deposit insurance reform is enacted, implement legislation in accordance with statutorily prescribed time frames.	Not Applicable. Legislation not enacted in 2004.
		Review discrepancies between projected failed assets and actual failed assets by applying sophisticated analytical techniques to examine the effectiveness of the loss projection model and adjust the methodology for projecting losses accordingly.	Achieved. See pgs. 8-9.
	Make appropriate changes to the current methodology for projecting losses in failing financial institutions and establishing related loss reserves for the deposit insurance funds.	Implement enhancements to the reserving process and methodology in accordance with recommendations from a comprehensive 2003 review.	Achieved. See pgs. 8-9.
	Maintain fund adequacy.	Set assessment rates to maintain the insurance funds at the designated reserve ratio, or return them to the designated reserve ratio if they fall below it, as required by statute.	Achieved. See pgs. 8-9.
		If deposit insurance reform legislation becomes law in 2004, promulgate rules and regulations establishing criteria for replenishing the deposit insurance fund when it falls below the low end of the range.	Not Applicable. Legislation not enacted in 2004.

**2004 Insurance Program Results** (continued)

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
4. Maintain and improve the deposit insurance system. (continued)		Develop a working prototype of a new, integrated fund model for financial risk management.	Achieved. See pgs. 8-9.
	Conduct a conference on the "Future of Banking."	Host conference, present findings from the study and obtain feedback from scholars and industry representatives and other interested parties.	Not Achieved. See pg. 28.
	Maintain quality and visibility of the Corporation's banking research activities.	Implement an FDIC Center for Financial Research with enhanced ties to the academic community.	Achieved. See pg. 10.
5. Provide educational information to insured depository institutions and their customers to help them understand the rules for determining the amount of insurance coverage on deposit accounts.	Utility of educational tools developed for bankers and consumers.	Develop a CD-ROM and Internet-based resource for bankers on the deposit insurance rules.	Achieved. See pg. 18.

**2004 Supervision and Consumer Protection Program Results**

**Strategic Goal: FDIC-supervised institutions are safe and sound.**

Annual Performance Goal	Indicator	Target	Results
1. Conduct on-site risk management examinations to assess an FDIC-supervised insured depository institution's overall financial condition, management practices and policies, and compliance with applicable laws and regulations.	Percentage of required examinations in accordance with statutory requirements and FDIC policy.	One hundred percent of required examinations are conducted on time.	Achieved. See pg. 12.
2. Take prompt supervisory actions to address problems found during the FDIC examination of FDIC-supervised institutions identified as problem insured depository institutions. Monitor FDIC-supervised insured depository institutions' compliance with formal and informal enforcement actions.	Follow-up examination of problem banks.	Follow-up examination is conducted within 12 months of completion of the prior examination.	Achieved. See pg. 12.



## 2004 Receivership Management Program Results

### Strategic Goal: Recovery to creditors of receiverships is achieved.

Annual Performance Goal	Indicator	Target	Results
1. Market failing institutions to all known qualified and interested potential bidders.	List of qualified and interested bidders.	Contact all known qualified and interested bidders.	Achieved. See pg. 19.
2. Value, manage, and market assets of failed institutions and their subsidiaries in a timely manner to maximize net return.	Percentage of failed institution's assets marketed.	Eighty-five percent of book value of a failed institution's marketable assets are marketed within 90 days of failure.	Achieved. See pg. 19.
3. Manage the receivership estate and its subsidiaries toward an orderly termination.	Timely termination of new receiverships.	Terminate 75 percent of receiverships managed through the Receivership Oversight Program within three years of the failure date.	Achieved. See pg. 20.
4. Conduct investigations into all potential professional liability claim areas in all failed insured depository institutions and decide as promptly as possible to close or pursue each claim, considering the size and complexity of the institution.	Percentage of investigated claim areas for which a decision has been made to close or pursue the claim.	For 80 percent of all claim areas, a decision is made to close or pursue the claim within 18 months after the failure date.	Achieved. See pg. 19.



## Prior Years Performance Results

(excerpted from the 2003 Annual Report) Page numbers refer to the 2003 report

### 2003 Insurance Program Results

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
1. Respond promptly to financial institution closings and emerging issues.	Number of business days after institution failure by which depositors will have access to insured funds either through transfer of deposits to successor insured depository institution or depositor payout.	If the failure occurs on a Friday, the target is one business day.  If the failure occurs on any other day of the week, the target is two business days.	Achieved.  Achieved.
2. Identify and address risks to the insurance funds.	Assess risks posed by large insured depository institutions.	Assess risks in 100 percent of large insured depository institutions and adopt appropriate strategies.	Achieved.
	Identify and follow up on concerns referred for examination or other action (i.e., contact the insured institutions or primary supervisor).	Identify and follow up on 100 percent of referrals.	Achieved.
	Disseminate data and analyses on current issues and risks affecting the banking industry to bankers, supervisors, stakeholders, and the public.	Analyses are included in regular publications or as ad hoc reports on a timely basis.	Achieved.
		Conduct industry outreach aimed at the banking community and industry trade groups to discuss current trends and concerns and to inform bankers about available FDIC resources.	Achieved.

**2003 Insurance Program Results** (continued)

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
<p>3. Maintain sufficient and reliable information on insured depository institutions.</p>	<p>Maintain and improve the Research Information System (RIS), which serves as the foundation of most analysis and statistical reporting for the FDIC.</p>	<p>Update and expand data availability in RIS.</p>	<p>Achieved.</p>
	<p>Develop a more efficient approach to bank data collection and management.</p>	<p>Determine Call Report Modernization system development approach; prepare migration plan for the implementation of data editing, storage and distribution facility for Call Report data; complete reconciliation of bank structure databases; and implement standard business rules and data definitions for Call Report information.</p>	<p>Achieved.</p>
<p>4. Maintain and improve the deposit insurance system.</p>	<p>Continue to pursue changes in the deposit insurance system in accordance with proposals submitted to Congress in 2002.</p>	<p>Work with Congress to develop and pass a reform package.</p>	<p>Not Achieved. See pgs. 12-13.</p>
		<p>Develop final pricing recommendations and implementation plans for inclusion in a notice-and-comment rulemaking during 2003.</p>	<p>Achieved.</p>
		<p>If deposit insurance reform is passed, implement legislation in a timely manner.</p>	<p>Not Applicable.</p>
		<p>Develop and analyze baseline data of implemented modification results.</p>	<p>Achieved.</p>
	<p>Continue to identify and review possible modifications to the Risk-Related Premium System (RRPS).</p>	<p>Assess improvements to the objective screens for the RRPS that identify financial institutions engaging in excessive risk taking, such as certain types of credit, market, and operational risks.</p>	<p>Achieved.</p>

**2003 Insurance Program Results** (continued)

**Strategic Goal: Insured depositors are protected from loss without recourse to taxpayer funding.**

Annual Performance Goal	Indicator	Target	Results
4. Maintain and improve the deposit insurance system. (continued)	Make appropriate changes to the current methodology for projecting losses in failing financial institutions and establishing related loss reserves for the deposit insurance funds.	Review discrepancies between projected failed assets and actual failed assets by applying sophisticated analytical techniques to examine the effectiveness of the loss projection model and adjust the methodology or projecting losses accordingly.	Achieved.
	Maintain fund adequacy.	Perform comprehensive review of all aspects of the reserving process and methodology and implement enhancements as necessary.	Achieved.
	Conduct a study on the "Future of Banking."	Set assessment rates to maintain the insurance funds at or above the designated reserve ratio, or to return them to the designated reserve ratio if they fall below it, as required by statute. If deposit insurance reform legislation becomes law in 2003, promulgate rules and regulations establishing criteria for replenishing the deposit insurance fund when it falls below the low end of the range.	Achieved.
	Enhance FDIC's ties to the academic community and upgrade and provide greater visibility to the Corporation's research activities.	Determine the implications of major trends for the evolution of the industry, development of regulatory policy and management of the deposit insurance funds.	Achieved.
5. Provide educational information to insured depository institutions and their customers to help them understand the rules for determining the amount of insurance coverage on deposit accounts.	Enhance the existing Electronic Deposit Insurance Estimator (EDIE) Banker version.	Issue a new version of the EDIE (Banker version) that accommodates corporate and organization accounts as well as any changes to the deposit insurance rules that may be adopted.	Achieved.

**2003 Supervision and Consumer Protection Program Results**

**Strategic Goal: FDIC-supervised institutions are safe and sound.**

Annual Performance Goal	Indicator	Target	Results
1. Conduct on-site safety and soundness examinations to assess an FDIC-supervised insured depository institution's overall financial condition, management practices and policies, and compliance with applicable regulations.	Conduct required examinations in accordance with statute and FDIC policy.	One hundred percent of required examinations are conducted on time.	Achieved.
2. Take prompt supervisory actions to address problems found during the FDIC examination of FDIC-supervised institutions identified as problem insured depository institutions. Monitor FDIC-supervised insured depository institution's compliance with formal and informal enforcement actions.	The number of months between last examination of a problem bank and follow-up examination.	Follow-up examination conducted within 12 months of completing the prior examination.	Achieved.

**Strategic Goal: Consumers' rights are protected and FDIC-supervised institutions invest in their communities.**

Annual Performance Goal	Indicator	Target	Results
1. Provide effective outreach and technical assistance on topics related to CRA, fair lending, and community development.	Additions to the <i>Money Smart</i> Alliance and the number of <i>Money Smart</i> curricula provided.	By December 31, 2003, cumulative totals of 400 <i>Money Smart</i> Alliance members and 40,000 <i>Money Smart</i> curricula provided.	Achieved.
	Outreach activities and technical assistance.	Conduct or participate in 125 <i>Money Smart</i> events, technical assistance efforts (examination support), or banker/community outreach activities related to CRA, fair lending, or community development.	Achieved.
2. Effectively meet the statutory mandate to investigate and respond to consumer complaints about FDIC-supervised financial institutions.	Timely responses to written complaints.	Ninety percent of written complaints are responded to within time frames established by policy.	Achieved.
3. Conduct comprehensive and compliance-only examinations in accordance with FDIC examination frequency policy.	Conduct required examinations in accordance with FDIC policy.	One hundred percent of required examinations are conducted within time frames established by FDIC policy.	Achieved.

**2003 Supervision and Consumer Protection Program Results** (continued)

**Strategic Goal: Consumers' rights are protected and FDIC-supervised institutions invest in their communities.**

Annual Performance Goal	Indicator	Target	Results
4. Take prompt supervisory actions and monitor all institutions rated "4" or "5" for compliance to address problems identified during compliance examinations.	Timely follow-up examination and related activity confirm whether the institution is in compliance with the enforcement action.	A follow-up examination or related activity is conducted within 12 months from the date of a formal enforcement action.	Achieved.

**2003 Receivership Management Program Results**

**Strategic Goal: Recovery to creditors of receiverships is achieved.**

Annual Performance Goal	Indicator	Target	Results
1. Market failing institutions to all known qualified and interested potential bidders.	List of qualified and interested bidders.	Contact all known qualified and interested bidders.	Achieved.
2. Value, manage, and market assets of failed institutions and their subsidiaries in a timely manner to maximize net return.	Failed institutions' assets marketed.	Eighty-five percent of book value of a failed institution's marketable assets are marketed within 90 days of failure.	Achieved.
3. Manage the receivership estate and its subsidiaries toward an orderly termination.	Timely termination of new receiverships.	Terminate 75 percent of receiverships managed through the Receivership Oversight Program within three years of the failure date.	Not Achieved. See pg. 19.
4. Conduct investigations into all potential professional liability claim areas in all failed insured depository institutions, and decide to close or pursue each claim as promptly as possible, considering the size and complexity of the institution.	Percentage of investigated claim areas for which a decision has been made to close or pursue the claim within 18 months after the failure date.	For 80 percent of all claim areas, a decision is made to close or pursue the claim.	Achieved.

## Program Evaluation

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The Corporation's 2006 Annual Performance Plan indicated that the FDIC would pursue the following Program Evaluation agenda in 2006:

**During 2006, considerable corporate resources will be devoted to implementing both program changes necessitated by Deposit Insurance Reform and the several changes in the automated systems supporting related activities. In addition, OERM (the Office of Enterprise Risk Management) will lead or participate in program evaluation activities in such areas as: risk management oversight on the development of new automated systems supporting our major programs; determining the continuing effectiveness of program areas that experienced significant downsizing in 2005; continuing implementation of balanced scorecards throughout the Corporation; and continuing our participation in performance management and monitoring efforts at the division/office level.**

As expected, the implementation of deposit insurance reform became the central focus of OERM's program evaluation efforts throughout 2006. In order to comply with the requirements of the Federal Deposit Insurance Reform Act of 2005 and the related Federal Deposit Insurance Reform Conforming Amendments Act of 2005, the FDIC had to analyze current business processes and operations in several program areas and to implement major changes in these programs by the end of the year. OERM program evaluation staff provided significant support in the documentation and analysis of current business processes.

In conjunction with the implementation of these program changes, the legislation also required the FDIC and the Government Accountability Office (GAO) to conduct a series of specific studies and targeted reviews/audits. Most significantly, the GAO was required to conduct an evaluation of the FDIC's overall structure and mission, with particular emphasis on the Corporation's frameworks for corporate governance, human capital management and risk management. This comprehensive, nine-month review encompassed all major FDIC programs and included operations at headquarters, regional and field offices. The review resulted in only two relatively minor recommendations, thus providing FDIC management with additional independent affirmation of the effectiveness of its existing corporate programs. The FDIC will complete its three studies in early 2007, covering "Accounting for Loss Contingencies: The FDIC's Policies and Practices 1992-2004," "An Evaluation of Further Possible Changes to the Deposit Insurance System," and "An Evaluation of the Denominator of the Reserve Ratio." The studies are scheduled to be delivered to Congress by February 15, 2007.

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Independent internal control staff in key divisions also continued to carry out traditional program and operational evaluations in 2006. These included continuing reviews of the Division of Supervision and Consumer Protection's regional and field office operations to ensure consistency and integrity of the FDIC's examination programs; and a review of payment and other controls in the Division of Resolutions and Receiverships to ensure the continued effectiveness and control of operations in the wake of the significant staff reductions made in 2005. OERM also continued its review of the Office of Diversity and Economic Opportunity to identify ways to improve the accuracy and timeliness of reporting.

*IV. Financial Statements and Notes*

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*Deposit Insurance Fund*



## Deposit Insurance Fund (combined BIF and SAIF for 2005 – Note 2)

Federal Deposit Insurance Corporation

### Deposit Insurance Fund Balance Sheet at December 31

Dollars in Thousands

	2006	2005
<b>Assets</b>		
Cash and cash equivalents	\$ 2,953,995	\$ 3,209,444
Cash and other assets: <i>Restricted for SAIF-member exit fees (Note 8)</i> <i>(Includes cash and cash equivalents of \$20.9 million at December 31, 2005)</i>	0	341,656
<i>Investment in U.S. Treasury obligations, net: (Note 3)</i>		
Held-to-maturity securities	37,184,214	34,253,237
Available-for-sale securities	8,958,566	9,987,223
Interest receivable on investments and other assets, net	747,715	737,566
Receivables from resolutions, net (Note 4)	538,991	533,474
Property and equipment, net (Note 5)	376,790	378,064
<b>Total Assets</b>	<b>\$ 50,760,271</b>	<b>\$ 49,440,664</b>
<b>Liabilities</b>		
Accounts payable and other liabilities	\$ 154,283	\$ 296,540
Postretirement benefit liability (Note 11)	129,906	0
<i>Contingent liabilities for: (Note 6)</i>		
Anticipated failure of insured institutions	110,775	5,366
Litigation losses	200,000	200,500
SAIF-member exit fees and investment proceeds held in escrow (Note 8)	0	341,656
<b>Total Liabilities</b>	<b>594,964</b>	<b>844,062</b>
<i>Commitments and off-balance-sheet exposure (Note 12)</i>		
<b>Fund Balance</b>		
Accumulated net income	49,929,226	48,190,062
Unrealized gain on available-for-sale securities, net (Note 3)	233,822	406,540
Unrealized postretirement benefit gain (Note 11)	2,259	0
<b>Total Fund Balance</b>	<b>50,165,307</b>	<b>48,596,602</b>
<b>Total Liabilities and Fund Balance</b>	<b>\$ 50,760,271</b>	<b>\$ 49,440,664</b>

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

## *Deposit Insurance Fund* (combined BIF and SAIF for 2005 – Note 2)

Federal Deposit Insurance Corporation

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

Dollars in Thousands

	2006	2005
<b>Revenue</b>		
Interest on U.S. Treasury obligations	\$ 2,240,723	\$ 2,341,505
Exit fees earned (Note 8)	345,295	0
Assessments (Note 7)	31,945	60,884
Other revenue	25,565	18,073
<b>Total Revenue</b>	<b>2,643,528</b>	<b>2,420,462</b>
<b>Expenses and Losses</b>		
Operating expenses (Note 9)	950,618	965,652
Provision for insurance losses (Note 10)	(52,097)	(160,170)
Insurance and other expenses	5,843	3,821
<b>Total Expenses and Losses</b>	<b>904,364</b>	<b>809,303</b>
<b>Net Income</b>		
	<b>1,739,164</b>	<b>1,611,159</b>
Unrealized loss on available-for-sale securities, net	(172,718)	(521,350)
Unrealized postretirement benefit gain	2,259	0
<b>Comprehensive Income</b>	<b>1,568,705</b>	<b>1,089,809</b>
<b>Fund Balance - Beginning</b>	<b>48,596,602</b>	<b>47,506,793</b>
<b>Fund Balance - Ending</b>	<b>\$ 50,165,307</b>	<b>\$ 48,596,602</b>

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

## Deposit Insurance Fund (combined BIF and SAIF for 2005 – Note 2)

Federal Deposit Insurance Corporation

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

Dollars in Thousands

	2006	2005
<b>Operating Activities</b>		
<b>Net Income:</b>	\$ 1,739,164	\$ 1,611,159
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of U.S. Treasury obligations	599,274	834,118
Treasury inflation-protected securities (TIPS) inflation adjustment	(109,394)	(345,023)
Depreciation on property and equipment	52,919	56,006
Provision for insurance losses	(52,097)	(160,170)
Terminations/adjustments of work-in-process accounts	433	178
Exit fees earned	(345,295)	0
<b>Change in Operating Assets and Liabilities:</b>		
Decrease/(Increase) in unamortized premium and discount of U.S. Treasury obligations (restricted)	1,359	(6,565)
(Increase)/Decrease in interest receivable and other assets	(14,635)	5,590
Decrease in receivables from resolutions	147,258	348,173
(Decrease)/Increase in accounts payable and other liabilities	(166,822)	27,145
Increase in postretirement benefit liability	129,906	0
(Decrease) in contingent liabilities for litigation losses	0	(182)
Increase in exit fees and investment proceeds held in escrow	3,639	28,556
<b>Net Cash Provided by Operating Activities</b>	<b>1,985,709</b>	<b>2,398,985</b>
<b>Investing Activities</b>		
<b>Provided by:</b>		
Maturity of U.S. Treasury obligations, held-to-maturity	5,955,000	8,220,000
Maturity of U.S. Treasury obligations, available-for-sale	845,000	1,830,000
<b>Used by:</b>		
Purchase of property and equipment	(11,721)	(47,197)
Purchase of U.S. Treasury obligations, held-to-maturity	(9,050,372)	(11,693,984)
<b>Net Cash Used by Investing Activities</b>	<b>(2,262,093)</b>	<b>(1,691,181)</b>
<b>Net (Decrease)/Increase in Cash and Cash Equivalents</b>	<b>(276,384)</b>	<b>707,804</b>
<b>Cash and Cash Equivalents - Beginning</b>	<b>3,230,379</b>	<b>2,522,575</b>
<b>Unrestricted Cash and Cash Equivalents - Ending</b>	<b>2,953,995</b>	<b>3,209,444</b>
<b>Restricted Cash and Cash Equivalents - Ending</b>	<b>0</b>	<b>20,935</b>
<b>Cash and Cash Equivalents - Ending</b>	<b>\$ 2,953,995</b>	<b>\$ 3,230,379</b>

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

## Deposit Insurance Fund

### Notes to the Financial Statements

December 31, 2006  
and 2005

## 1. Legislation and Operations of the Deposit Insurance Fund

### Overview

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

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

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

### Recent Legislation

The Federal Deposit Insurance Reform Act of 2005 (Reform Act [Title II, Subtitle B of Public Law 109-171, 120 Stat. 9]) was enacted on February 8, 2006. Companion legislation, the Federal Deposit Insurance Reform Conforming Amendments Act of 2005 (Public Law 109-173, 119 Stat. 3601), was enacted on February 15, 2006. In addition to merging the BIF and the SAIF, the legislation: 1) requires the deposit of funds into the DIF for SAIF-member exit fees that had been restricted and held in escrow; 2) provides FDIC with greater discretion to charge insurance assessments and to impose more sensitive risk-based pricing; 3) annually permits the designated reserve ratio to vary between 1.15 and 1.50 percent of estimated insured deposits, thereby eliminating the statutorily fixed designated reserve ratio of 1.25 percent; 4) generally requires the declaration and payment of dividends from the DIF if the reserve ratio of the DIF equals or exceeds 1.35 percent of estimated insured deposits at the end of a calendar year; 5) grants a one-time assessment credit for each eligible insured depository

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institution or its successor based on an institution's proportionate share of the aggregate assessment base of all eligible institutions at December 31, 1996; and 6) immediately increases coverage for certain retirement accounts to \$250,000 and allows the FDIC to increase all deposit insurance coverage, under certain circumstances, to reflect inflation every five years beginning January 1, 2011. See Note 7 for a more detailed discussion of these reforms.

### **Operations of the DIF**

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

The DIF is primarily funded from: 1) interest earned on investments in U.S. Treasury obligations and 2) deposit insurance assessments. Additional funding sources, if necessary, are borrowings from the U.S. Treasury, Federal Financing Bank, Federal Home Loan Banks, and insured depository institutions. The FDIC has borrowing authority from the U.S. Treasury up to \$30 billion for insurance purposes on behalf of the DIF. On December 15, 2006, the FDIC entered into a Note Purchase Agreement with the Federal Financing Bank in an amount not exceeding \$40 billion. The Note Purchase Agreement, if needed, will enhance DIF's ability to fund large deposit insurance obligations and deal with large institution resolutions.

A statutory formula, known as the Maximum Obligation Limitation (MOL), limits the amount of obligations the DIF can incur to the sum of its cash, 90 percent of the fair market value of other assets, and the amount authorized to be borrowed from the U.S. Treasury. The MOL for the DIF was \$79.7 billion and \$78.2 billion as of December 31, 2006 and 2005, respectively.

### **Receivership Operations**

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

## 2. Summary of Significant Accounting Policies

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### General

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

### Merger of the Funds

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The merger of the BIF and SAIF into the newly established DIF was accounted for by combining the carrying value of each Fund's assets and liabilities. Since this merger results in a new reporting entity, financial results of the newly formed DIF were retrospectively applied as though they had been combined at the beginning of the reporting year as well as for full prior year periods reported for comparative purposes.

### Use of Estimates

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

### Cash Equivalents

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

### Investment in U.S. Treasury Obligations

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

DIF's investments in U.S. Treasury obligations are either classified as held-to-maturity or available-for-sale. Securities designated as held-to-maturity are shown at amortized cost. Amortized cost is the face value of securities plus the unamortized premium or less the unamortized discount. Amortizations are

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computed on a daily basis from the date of acquisition to the date of maturity, except for callable U.S. Treasury securities, which are amortized to the first call date. Securities designated as available-for-sale are shown at market value, which approximates fair value. Unrealized gains and losses are included in Comprehensive Income. Realized gains and losses are included in the Statement of Income and Fund Balance as components of Net Income. Income on both types of securities is calculated and recorded on a daily basis using the effective interest method.

### **Capital Assets and Depreciation**

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

### **Disclosure about Recent Accounting Pronouncements**

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In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106, and 132(R)*. For FDIC's postretirement benefits other than pensions, this pronouncement amends the recognition and disclosure requirements of SFAS No. 106 and SFAS No. 132(R).

The pronouncement requires recognition of: 1) the funded status of the plan as an asset or liability, 2) the cumulative actuarial gains/losses and prior service costs/credits as accumulated comprehensive income, and 3) the changes in the actuarial gains/losses and prior service costs/credits for the period as other comprehensive income. The FDIC adopted SFAS No. 158 for the 2006 calendar year financial statements. As a result, the FDIC recognized the underfunded status (difference between the accumulated postretirement benefit obligation and the plan assets at fair value) as a liability and the cumulative actuarial gains/losses and prior service costs/credits are shown as accumulated other comprehensive income on the Balance Sheet. In addition, the changes in the actuarial gains/losses and prior service costs/credits for the period are recognized as other comprehensive income on the Statement of Income and Fund Balance. Prior to this change, the net postretirement benefit obligation (comprised of both the underfunded status and unrecognized actuarial gains/losses and prior service costs/credits) was recognized as a liability on the Balance Sheet.

Retrospective application is not permitted or required by the Statement. See Note 11 for specifics regarding postretirement benefits other than pensions.

### **Related Parties**

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

## Deposit Insurance Fund

### 3. Investment in U.S. Treasury Obligations, Net

As of December 31, 2006 and 2005, the book value of investments in U.S. Treasury obligations, net, was \$46.1 billion and \$44.2 billion, respectively. As of December 31, 2006, the DIF held \$9.2 billion of Treasury inflation-protected securities (TIPS). These securities are indexed to increases or decreases in the Consumer Price Index for All Urban Consumers (CPI-U). Additionally, the DIF held \$6.1 billion of callable U.S. Treasury bonds at December 31, 2006. Callable U.S. Treasury bonds may be called five years prior to the respective bonds' stated maturity on their semi-annual coupon payment dates upon 120 days notice.

#### U.S. Treasury Obligations at December 31, 2006

Dollars in Thousands

Maturity <sup>•</sup>	Yield at Purchase <sup>▼</sup>	Face Value	Net Carrying Amount	Unrealized Holding Gains	Unrealized Holding Losses <sup>■</sup>	Market Value
<b>Held-to-Maturity</b>						
<b>U. S. Treasury notes and bonds</b>						
Within 1 year	4.58%	\$ 6,401,000	\$ 6,448,905	\$ 3,389	\$ (20,704)	\$ 6,431,590
After 1 year thru 5 years	4.47%	15,500,000	16,276,424	91,703	(196,635)	16,171,492
After 5 years thru 10 years	4.68%	9,025,000	9,690,085	36,025	(42,270)	9,683,840
After 10 years	5.01%	2,445,000	3,247,814	57,589	(3,227)	3,302,176
<b>U. S. Treasury inflation-protected securities</b>						
After 1 year thru 5 years	3.83%	926,751	926,844	21,185	0	948,029
After 5 years thru 10 years	2.41%	568,345	594,142	0	(778)	593,364
<b>Total</b>		<b>\$ 34,866,096</b>	<b>\$ 37,184,214</b>	<b>\$ 209,891</b>	<b>\$ (263,614)</b>	<b>\$ 37,130,491</b>

#### Available-for-Sale

<b>U. S. Treasury notes and bonds</b>						
Within 1 year	3.85%	\$ 1,225,000	\$ 1,269,835	\$ 0	\$ (9,208)	\$ 1,260,627
<b>U. S. Treasury inflation-protected securities</b>						
After 1 year thru 5 years	3.80%	7,443,478	7,454,909	243,030	0	7,697,939
<b>Total</b>		<b>\$ 8,668,478</b>	<b>\$ 8,724,744</b>	<b>\$ 243,030</b>	<b>\$ (9,208)</b>	<b>\$ 8,958,566</b>

#### Total Investment in U.S. Treasury Obligations, Net

<b>Total</b>		<b>\$ 43,534,574</b>	<b>\$ 45,908,958</b>	<b>\$ 452,921</b>	<b>\$ (272,822)</b>	<b>\$ 46,089,057</b>
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<sup>•</sup> For purposes of this table, all callable securities are assumed to mature on their first call dates. Their yields at purchase are reported as their yield to first call date.

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

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



## U.S. Treasury Obligations at December 31, 2005

Dollars in Thousands

Maturity*	Yield at Purchase <sup>†</sup>	Face Value	Net Carrying Amount	Unrealized Holding Gains	Unrealized Holding Losses <sup>‡</sup>	Market Value
<b>Held-to-Maturity</b>						
<b>U . S. Treasury notes and bonds</b>						
Within 1 year	5.19%	\$ 5,920,000	\$ 5,942,398	\$ 29,554	\$ (18,187)	\$ 5,953,765
After 1 year thru 5 years	4.47%	18,680,000	19,872,850	219,864	(187,672)	19,905,042
After 5 years thru 10 years	4.53%	5,350,000	5,674,953	62,578	(13,184)	5,724,347
After 10 years	4.72%	1,420,000	1,848,524	31,668	0	1,880,192
<b>U . S. Treasury inflation-protected securities</b>						
After 1 year thru 5 years	3.83%	914,596	914,512	40,784	0	955,296
<b>Total</b>		<b>\$ 32,284,596</b>	<b>\$ 34,253,237</b>	<b>\$ 384,448</b>	<b>\$ (219,043)</b>	<b>\$ 34,418,642</b>

### Available-for-Sale

<b>U . S. Treasury notes and bonds</b>						
Within 1 year	3.71%	\$ 845,000	\$ 898,720	\$ 696	\$ (6,870)	\$ 892,546
After 1 year thru 5 years	3.86%	1,225,000	1,324,055	4,967	(16,448)	1,312,574
<b>U . S. Treasury inflation-protected securities</b>						
After 1 year thru 5 years	3.97%	5,119,864	5,122,414	280,679	0	5,403,093
After 5 years thru 10 years	3.39%	2,225,975	2,235,494	143,516	0	2,379,010
<b>Total</b>		<b>\$ 9,415,839</b>	<b>\$ 9,580,683</b>	<b>\$ 429,858</b>	<b>\$ (23,318)</b>	<b>\$ 9,987,223</b>

### Total Investment in U.S. Treasury Obligations, Net

<b>Total</b>	<b>\$ 41,700,435</b>	<b>\$ 43,833,920</b>	<b>\$ 814,306</b>	<b>\$ (242,361)</b>	<b>\$ 44,405,865</b>
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\* For purposes of this table, all callable securities are assumed to mature on their first call dates. Their yields at purchase are reported as their yield to first call date.

† For TIPS, the yields in the above table are stated at their real yields at purchase, not their effective yields. Effective yields on TIPS include a long-term annual inflation assumption as measured by the CPI-U. The long-term CPI-U consensus forecast is 2.2 percent, based on figures issued by the Congressional Budget Office and *Blue Chip Economic Indicators* in early 2005.

‡ All unrealized losses occurred as a result of changes in market interest rates. FDIC has the ability and intent to hold the related securities until maturity. As a result, all unrealized losses are considered temporary. However, of the \$242 million reported as total unrealized losses, \$116 million is recognized as unrealized losses occurring

As of December 31, 2006 and 2005, the unamortized premium, net of the unamortized discount, was \$2.4 billion and \$2.1 billion, respectively.

### **4** 4. Receivables From Resolutions, Net

The receivables from resolutions include payments made by the DIF to cover obligations to insured depositors, advances to receiverships for working capital, and administrative expenses paid on behalf of receiverships. Any related allowance for loss represents the difference between the funds advanced and/or obligations incurred and the expected repayment. Assets held by DIF receiverships are the main source of repayment of the DIF's receivables from closed banks and thrifts. As of December 31, 2006, there were 25 active receiverships, with no failures in the current year.

As of December 31, 2006 and 2005, DIF receiverships held assets with a book value of \$655 million and \$745 million, respectively (including cash, investments, and miscellaneous receivables of \$348 million and \$370 million at December 31, 2006 and 2005, respectively). The estimated cash recoveries from the management and disposition of these assets that are used to derive the allowance for losses are based on a sampling of receivership assets in liquidation. Assets in the judgmental sample, which represents 97 percent of the asset book value for all active DIF receiverships, are generally valued by estimating future cash recoveries, net of applicable liquidation cost estimates, and then discounting these net cash recoveries using current market-based risk factors based on a given asset's type and quality. Resultant recovery estimates are extrapolated to the non-sampled assets in order to derive the allowance for loss on the receivable. These estimated recoveries are regularly evaluated, but remain subject to uncertainties because of potential changes in economic and market conditions. Such uncertainties could cause the DIF's actual recoveries to vary from the level currently estimated.

As of December 31, 2006, the DIF allowance for loss was \$4.1 billion. The allowance for loss is equivalent to 88 percent of the gross receivable. Of the remaining 12 percent of the gross receivable, the amount of credit risk is limited since 89.1 percent of the receivable will be repaid from receivership cash, investments, and a promissory note fully secured by a letter of credit.

## 5. Property and Equipment, Net

### Property and Equipment, Net at December 31

Dollars in Thousands

	2006	2005
Land	\$ 37,352	\$ 37,352
Buildings (includes construction-in-process)	284,871	272,861
Application software (includes work-in-process)	259,744	241,424
Furniture, fixtures, and equipment	161,127	140,728
Accumulated depreciation	(323,274)	(273,789)
Retirements	(43,030)	(40,512)
<b>Total</b>	<b>\$ 376,790</b>	<b>\$ 378,064</b>

The depreciation expense was \$53 million and \$56 million for December 31, 2006 and 2005, respectively.

## 6. Contingent Liabilities for:

### Anticipated Failure of Insured Institutions

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

The contingent liability is derived by applying expected failure rates and loss rates to institutions based on supervisory ratings, balance sheet characteristics, and projected capital levels. In addition, institution-specific analysis is performed on those institutions where failure is imminent absent institution management resolution of existing problems, or where additional information is available that may affect the estimate of losses. As of December 31, 2006 and 2005, the contingent liabilities for anticipated failure of insured institutions were \$110.8 million and \$5.4 million, respectively.

In addition to these recorded contingent liabilities, the FDIC has identified additional risk in the financial services industry that could result in an additional loss to the DIF should potentially vulnerable insured institutions ultimately fail. This risk results from the presence of various high-risk banking business activities that are particularly vulnerable to adverse economic and market conditions. Due to the uncertainty surrounding such conditions in the future, there are institutions other than those with losses included in the contingent liability for which the risk of failure is less certain, but still considered reasonably possible. As a result of these risks, the FDIC believes that it is reasonably possible that the DIF could incur additional estimated losses up to approximately \$0.6 billion.

## *Deposit Insurance Fund*

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The accuracy of these estimates will largely depend on future economic and market conditions. The FDIC's Board of Directors has the statutory authority to consider the contingent liability from anticipated failures of insured institutions when setting assessment rates.

### **Litigation Losses**

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

### **Other Contingencies**

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#### ***Representations and Warranties***

As part of the FDIC's efforts to maximize the return from the sale of assets from bank and thrift resolutions, representations and warranties, and guarantees were offered on certain loan sales. In general, the guarantees, representations, and warranties on loans sold relate to the completeness and accuracy of loan documentation, the quality of the underwriting standards used, the accuracy of the delinquency status when sold, and the conformity of the loans with characteristics of the pool in which they were sold. The total amount of loans sold subject to unexpired representations and warranties, and guarantees was \$8.1 billion as of December 31, 2006. There were no contingent liabilities from any of the outstanding claims asserted in connection with representations and warranties at December 31, 2006 and 2005, respectively.

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

## **7. Assessments**

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The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) required the FDIC to establish a risk-based assessment system, charging higher rates to those insured depository institutions that posed greater risks to the DIF. To arrive at a risk-based assessment for a particular institution, the FDIC placed each institution in one of nine risk categories based on capital ratios and supervisory examination data. Based on FDIC's evaluation of the institutions under the risk-based premium system and due to limitations imposed by the

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Deposit Insurance Funds Act of 1996 (DIFA) and the continued health of the banking and thrift industries, most institutions were not charged an assessment for a number of years. In addition, the FDIC was required by statute to maintain the insurance funds at a designated reserve ratio (DRR) of not less than 1.25 percent of estimated insured deposits (or a higher percentage as circumstances warranted). Of the institutions assessed, the assessment rate averaged approximately 5 cents and 10 cents per \$100 of assessable deposits for 2006 and 2005, respectively. During 2006 and 2005, \$32 million and \$61 million were recognized as assessment income from institutions, respectively.

The assessment process will significantly change as of January 1, 2007. The Reform Act (enacted in February 2006) and the implementing regulations (published in November 2006):

- provide the FDIC with greater discretion to charge insurance assessments, eliminate the cap on assessments for the best-rated institutions, and provide that no insured institution may be barred from the lowest risk category solely because of its size. By regulation, the FDIC has placed each institution into one of four risk categories for risk-based assessment purposes, so that all insured depository institutions will be required to pay assessments;
- establish a range for the DRR from 1.15 to 1.50 percent of estimated insured deposits and eliminate the fixed DRR of 1.25 percent. The FDIC is required to annually publish the DRR and has, by regulation, set the DRR at 1.25 percent for 2007;
- grant a one-time assessment credit of approximately \$4.7 billion to certain eligible insured depository institutions (or their successors) based on the assessment base of the institution as of December 31, 1996, as compared to the combined aggregate assessment base of all eligible institutions; and
- require the FDIC to annually determine if a dividend should be paid, based on the statutory requirements generally to declare dividends if: 1) the reserve ratio of the DIF exceeds 1.50 percent of estimated insured deposits, for the full amount in excess of the amount required to maintain the reserve ratio at 1.50 percent, or 2) if the reserve ratio equals or exceeds 1.35 percent of estimated insured deposits but is no greater than 1.50 percent, for one-half of the amount in excess of the amount required to maintain the reserve ratio at 1.35 percent.

Assessments continue to be levied on institutions for payments of the interest on obligations issued by the Financing Corporation (FICO). The FICO was established as a mixed-ownership government corporation to function solely as a financing vehicle for the FSLIC. The annual FICO interest obligation of approximately \$790 million is paid on a pro rata basis using the same rate for banks and thrifts. The FICO assessment has no financial impact on the DIF and is separate from deposit insurance assessments. The FDIC, as administrator of the DIF, acts solely as a collection agent for the FICO. During 2006 and 2005, \$788 million and \$780 million, respectively, were collected and remitted to the FICO.

### **8. Exit Fees Earned**

From the early to mid-1990s, the SAIF collected entrance and exit fees for conversion transactions when an insured depository institution converted from the BIF to the SAIF (resulting in an entrance fee) or from the SAIF to the BIF (resulting in an exit fee). Regulations approved by the FDIC's Board of Directors (Board) and published in the *Federal Register* on March 21, 1990, directed that: 1) exit fees paid to the SAIF be held in escrow, and 2) the Board and the Secretary of the Treasury will determine when it is no longer necessary to escrow such funds for the payment of interest on obligations previously issued by the FICO. These escrowed exit fees were invested in U.S. Treasury securities pending determination of ownership. The interest earned was also held in escrow and as a result of the above, the SAIF did not recognize exit fees or any interest earned as revenue.

The recent deposit insurance legislation removed the restriction on SAIF-member exit fees held in escrow and the funds were deposited into the general (unrestricted) fund of the DIF. The exit fees plus earned interest, a total of \$345 million, are recognized as revenue at their carrying value on the Income Statement for 2006 and are classified on the Balance Sheet as a combination of Cash and cash equivalents, Investments in U.S. Treasury obligations, net, and Interest receivable on investments. At December 31, 2005, the exit fees and earned interest are shown on the Balance Sheet line items of Cash and other assets: Restricted for SAIF-member exit fees (an asset) and SAIF-member exit fees and investment proceeds held in escrow (a liability).

## 9. Operating Expenses

Operating expenses were \$951 million for 2006, compared to \$966 million for 2005. The chart below lists the major components of operating expenses.

### Operating Expenses for the Years Ended December 31

Dollars in Thousands

	2006	2005
Salaries and benefits	\$ 619,452	\$ 645,418
Outside services	124,045	113,416
Travel	49,408	45,732
Buildings and leased space	65,929	71,480
Software/Hardware maintenance	27,139	33,366
Depreciation of property and equipment	52,919	55,989
Other	22,124	21,959
Services billed to receiverships	(10,398)	(21,708)
<b>Total</b>	<b>\$ 950,618</b>	<b>\$ 965,652</b>

## 10. Provision for Insurance Losses

Provision for insurance losses was a negative \$52 million for 2006 and a negative \$160 million for 2005. The following chart lists the major components of the provision for insurance losses.

### Provision for Insurance Losses for the Years Ended December 31

Dollars in Thousands

	2006	2005
<b>Valuation Adjustments:</b>		
Closed banks and thrifts	\$ (152,776)	\$ (159,421)
Other assets	(4,230)	3,762
<b>Total Valuation Adjustments</b>	<b>(157,006)</b>	<b>(155,659)</b>
<b>Contingent Liabilities Adjustments:</b>		
Anticipated failure of insured institutions	105,409	(4,852)
Litigation losses	(500)	200
Other contingencies	0	141
<b>Total Contingent Liabilities Adjustments</b>	<b>104,909</b>	<b>(4,511)</b>
<b>Total</b>	<b>\$ (52,097)</b>	<b>\$ (160,170)</b>

## Deposit Insurance Fund

### 11. Employee Benefits

#### Pension Benefits, Savings Plans and Postemployment Benefits

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

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

Prior to 2006, the FDIC reduced its workforce with a voluntary buyout program, and to a lesser extent, reduction-in-force actions resulting in separation or severance payments. The 2006 and 2005 related costs for these reductions are included in the "Operating expenses" line item in the Income Statement.

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

Dollars in Thousands

	2006	2005
Civil Service Retirement System	\$ 6,808	\$ 7,632
Federal Employees Retirement System (Basic Benefit)	38,915	38,458
FDIC Savings Plan	20,681	20,886
Federal Thrift Savings Plan	15,328	15,228
Separation Incentive Payment	0	22,371
Severance Pay	39	2,733
<b>Total</b>	<b>\$ 81,771</b>	<b>\$ 107,308</b>



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### **Postretirement Benefits Other Than Pensions**

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

At December 31, 2006, the DIF's accumulated postretirement benefit obligation, representing the underfunded status of the plan, was \$129.9 million, which is recognized in the "Postretirement benefit liability" line item on the Balance Sheet. The cumulative actuarial gains/losses (changes in assumptions and plan experience) and prior service costs/credits (changes to plan provisions that increase or decrease benefits) was \$2.3 million at December 31, 2006, which is reported as accumulated other comprehensive income in the "Unrealized postretirement benefit gain" line item on the Balance Sheet. At December 31, 2005, the net postretirement benefit liability (the underfunded status adjusted for any unrecognized actuarial gains/losses and prior service costs/credits) of \$126.7 million is recognized in the "Accounts payable and other liabilities" line item.

The DIF's expense for postretirement benefits in 2006 and 2005 was \$9.0 million and \$10.3 million, respectively, which is included in the current and prior year's operating expenses on the Statement of Income and Fund Balance. The changes in the actuarial gains/losses and prior service costs/credits for 2006 of \$2.3 million are reported as other comprehensive income in the "Unrealized postretirement benefit gain" line item. Key actuarial assumptions used in the accounting for the plan include the discount rate of 4.75 percent, the rate of compensation increase of 4.00 percent, and the dental coverage trend rate of 6.70 percent. See Note 2 regarding the recent issuance of a relevant FASB accounting pronouncement.

## Deposit Insurance Fund

# 12

## 12. Commitments and Off-Balance-Sheet Exposure

### Commitments:

#### *Leased Space*

The FDIC's lease commitments total \$62.9 million for future years. The lease agreements contain escalation clauses resulting in adjustments, usually on an annual basis. The DIF recognized leased space expense of \$30 million and \$39 million for the periods ended December 31, 2006 and 2005, respectively.

#### Leased Space Commitments

Dollars in Thousands

2007	2008	2009	2010	2011	2012/Thereafter
\$ 21,491	\$ 15,723	\$ 13,552	\$ 6,334	\$ 3,727	\$ 2,026

### Off-Balance-Sheet Exposure:

#### *Deposit Insurance*

As of September 30, 2006, the estimated insured deposits for DIF were \$4.1 trillion. This estimate is derived primarily from quarterly financial data submitted by insured depository institutions to the FDIC. This estimate represents the accounting loss that would be realized if all insured depository institutions were to fail and the acquired assets provided no recoveries.

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# 13

## **13. Disclosures About the Fair Value of Financial Instruments**

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

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

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

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

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*FSLIC Resolution Fund*

## Federal Deposit Insurance Corporation

**FSLIC Resolution Fund Balance Sheet at December 31**

Dollars in Thousands

	2006	2005
<b>Assets</b>		
Cash and cash equivalents	\$ 3,616,466	\$ 3,602,703
Receivables from thrift resolutions and other assets, net (Note 3)	36,730	38,746
Receivables from U.S. Treasury for goodwill judgments (Note 4)	251,827	0
<b>Total Assets</b>	<b>\$ 3,905,023</b>	<b>\$ 3,641,449</b>
<b>Liabilities</b>		
Accounts payable and other liabilities	\$ 5,497	\$ 7,799
Contingent liabilities for litigation losses and other (Note 4)	279,327	257,503
<b>Total Liabilities</b>	<b>284,824</b>	<b>265,302</b>
<b>Resolution Equity (Note 5)</b>		
Contributed capital	127,453,996	127,007,441
Accumulated deficit	(123,833,797)	(123,631,294)
<b>Total Resolution Equity</b>	<b>3,620,199</b>	<b>3,376,147</b>
<b>Total Liabilities and Resolution Equity</b>	<b>\$ 3,905,023</b>	<b>\$ 3,641,449</b>

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

## *FSLIC Resolution Fund*

Federal Deposit Insurance Corporation

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

Dollars in Thousands

	2006	2005
<b>Revenue</b>		
Interest on U.S. Treasury obligations	\$ 151,648	\$ 98,260
Other revenue	17,650	24,176
<b>Total Revenue</b>	<b>169,298</b>	<b>122,436</b>
<b>Expenses and Losses</b>		
Operating expenses	12,002	24,626
Provision for losses	(19,257)	(16,112)
Goodwill/Guarini litigation expenses (Note 4)	411,056	975,598
Recovery of tax benefits	(34,783)	(45,946)
Other expenses	2,783	10,333
<b>Total Expenses and Losses</b>	<b>371,801</b>	<b>948,499</b>
<b>Net (Loss)</b>	<b>(202,503)</b>	<b>(826,063)</b>
<b>Accumulated Deficit - Beginning</b>	<b>(123,631,294)</b>	<b>(122,805,231)</b>
<b>Accumulated Deficit - Ending</b>	<b>\$ (123,833,797)</b>	<b>\$ (123,631,294)</b>

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

## Federal Deposit Insurance Corporation

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

Dollars in Thousands

	2006	2005
<b>Operating Activities</b>		
<b>Net (Loss)</b>	\$ (202,503)	\$ (826,063)
Adjustments to reconcile net (loss) to net cash (used by) operating activities:		
Provision for losses	(19,257)	(16,112)
<b>Change in Assets and Liabilities:</b>		
Decrease in receivables from thrift resolutions and other assets	21,273	59,630
(Decrease)/Increase in accounts payable and other liabilities	(2,302)	2,196
Increase in contingent liabilities for litigation losses and other	21,824	257,104
<b>Net Cash (Used by) Operating Activities</b>	<b>(180,965)</b>	<b>(523,245)</b>
<b>Financing Activities</b>		
<b>Provided by:</b>		
U.S. Treasury payments for goodwill litigation	194,728	624,564
<b>Net Cash Provided by Financing Activities</b>	<b>194,728</b>	<b>624,564</b>
<b>Net Increase in Cash and Cash Equivalents</b>	<b>13,763</b>	<b>101,319</b>
<b>Cash and Cash Equivalents - Beginning</b>	<b>3,602,703</b>	<b>3,501,384</b>
<b>Cash and Cash Equivalents - Ending</b>	<b>\$ 3,616,466</b>	<b>\$ 3,602,703</b>

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

## *FSLIC Resolution Fund*

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### Notes to the Financial Statements

December 31, 2006  
and 2005

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

#### **Legislative History**

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

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

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

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



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### **Operations/Dissolution of the FRF**

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

The FDIC has conducted an extensive review and cataloging of FRF's remaining assets and liabilities and is continuing to explore approaches for concluding FRF's activities. An executive-level Steering Committee was established in 2003 to facilitate the FRF dissolution. Some of the issues and items that remain open in FRF are: 1) criminal restitution orders (generally have from 5 to 10 years remaining to enforce); 2) collections of settlements and judgments obtained against officers and directors and other professionals responsible for causing or contributing to thrift losses (generally have from 6 months to 12 years remaining to enforce); 3) numerous assistance agreements entered into by the former FSLIC (FRF could continue to receive tax-sharing benefits through year 2008); 4) goodwill and Guarini litigation (no final date for resolution has been established; see Note 4); and 5) environmentally impaired owned real estate assets. The FDIC is considering whether enabling legislation or other measures may be needed to accelerate liquidation of the remaining FRF assets and liabilities. The FRF could realize substantial recoveries from the tax-sharing benefits, criminal restitution orders and professional liability claims ranging from \$165 million to \$271.4 million; however, any associated recoveries are not reflected in FRF's financial statements given the significant uncertainties surrounding the ultimate outcome.

### **Receivership Operations**

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

## **2** **2. Summary of Significant Accounting Policies**

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### **General**

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

### **Use of Estimates**

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

### **Provision for Losses**

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

### **Fair Value of Financial Instruments**

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

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

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

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**Disclosure About Recent Accounting Pronouncements**

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Recent accounting pronouncements have been adopted or deemed to be not applicable to the financial statements as presented.

**Related Parties**

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

**Reclassifications**

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Reclassifications have been made in the 2005 financial statements to conform to the presentation used in 2006.

**3****3. Receivables From Thrift Resolutions and Other Assets, Net**

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**Receivables From Thrift Resolutions**

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The receivables from thrift resolutions include payments made by the FRF to cover obligations to insured depositors, advances to receiverships for working capital, and administrative expenses paid on behalf of receiverships. Any related allowance for loss represents the difference between the funds advanced and/or obligations incurred and the expected repayment. Assets held by the FDIC in its receivership capacity for the former FSLIC and SAIF-insured institutions are a significant source of repayment of the FRF's receivables from thrift resolutions. As of December 31, 2006, 20 of the 850 FRF receiverships remain active primarily due to unresolved litigation, including goodwill matters.

As of December 31, 2006 and 2005, FRF receiverships held assets with a book value of \$33 million and \$139 million, respectively (including cash, investments, and miscellaneous receivables of \$26 million and \$113 million at December 31, 2006 and 2005, respectively). The estimated cash recoveries from the management and disposition of these assets that are used to derive the allowance for losses are based on a sampling of receivership assets in liquidation. Assets in the judgmental sample, which represents 96 percent of the asset book value for all active FRF receiverships, are generally valued by estimating future cash recoveries, net of applicable liquidation cost estimates, and then discounting these net cash recoveries using current market-based risk factors based on a given asset's type and quality. Resultant recovery estimates are extrapolated to the non-sampled assets in order to derive the allowance for loss on the receivable. These estimated recoveries are regularly evaluated, but remain subject to uncertainties because of potential changes in economic and market conditions. Such uncertainties could cause the FRF's actual recoveries to vary from the level currently estimated.

## *FSLIC Resolution Fund*

### **Other Assets**

Other assets primarily include credit enhancement reserves valued at \$20.2 million and \$16.7 million as of December 31, 2006 and 2005, respectively. The credit enhancement reserves resulted from swap transactions where the former RTC received mortgage-backed securities in exchange for single-family mortgage loans. The RTC supplied credit enhancement reserves for the mortgage loans in the form of cash collateral to cover future credit losses over the remaining life of the loans. These reserves may cover future credit losses through 2020.

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

Dollars in Thousands

	<b>2006</b>	<b>2005</b>
Receivables from closed thrifts	\$ 11,308,460	\$ 16,080,789
Allowance for losses	(11,299,448)	(16,065,703)
<b>Receivables from Thrift Resolutions, Net</b>	<b>9,012</b>	<b>15,086</b>
Other assets	27,718	23,660
<b>Total</b>	<b>\$ 36,730</b>	<b>\$ 38,746</b>

Gross receivables from thrift resolutions subject the FRF to credit risk. An allowance for loss of \$11.3 billion, or 99.9 percent of the gross receivable, was recorded as of December 31, 2006. Of the remaining 0.1 percent of the gross receivable, 65 percent is expected to be repaid from receivership cash and investments.

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## 4 4. Contingent Liabilities for:

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### Litigation Losses

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The FRF records an estimated loss for unresolved legal cases to the extent those losses are considered probable and reasonably estimable. In addition to the amount recorded as probable, the FDIC has determined that losses from unresolved legal cases totaling \$3 million are reasonably possible.

### Additional Contingency

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#### *Goodwill Litigation*

In *United States v. Winstar Corp.*, 518 U.S. 839 (1996), the Supreme Court held that when it became impossible following the enactment of FIRREA in 1989 for the federal government to perform certain agreements to count goodwill toward regulatory capital, the plaintiffs were entitled to recover damages from the United States. Approximately 26 remaining cases are pending against the United States based on alleged breaches of these agreements.

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

The goodwill lawsuits are against the United States and as such are defended by the DOJ. On November 15, 2006, the DOJ again informed the FDIC that it is "unable at this time to provide a reasonable estimate of the likely aggregate contingent liability resulting from the *Winstar*-related cases." This uncertainty arises, in part, from the existence of significant unresolved issues pending at the appellate or trial court level, as well as the unique circumstances of each case.

## ***FSLIC Resolution Fund***

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

The FRF paid \$194.7 million as a result of judgments and settlements in four goodwill cases for the year ended December 31, 2006, compared to \$624.6 million for seven goodwill cases for the year ended December 31, 2005. As described above, the FRF received appropriations from the U.S. Treasury to fund these payments. At December 31, 2006, the FRF accrued a \$251.8 million contingent liability and offsetting receivable from the U.S. Treasury for judgments in two additional cases that were fully adjudicated as of year end. These funds were paid in January 2007.

In addition, the FRF-FSLIC pays the goodwill litigation expenses incurred by DOJ based on a Memorandum of Understanding (MOU) dated October 2, 1998, between the FDIC and DOJ. Under the terms of the MOU, the FRF-FSLIC paid \$17.5 million and \$18.3 million to DOJ for fiscal years (FY) 2007 and 2006, respectively. DOJ returns any unused fiscal year funding to the FRF unless special circumstances warrant these funds be carried over and applied against current fiscal year charges. At September 30, 2006, DOJ had an additional \$3.4 million in unused fiscal year 2006 funds that were applied against FY 2007 charges of \$20.9 million.

### ***Guarini Litigation***

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

Eight Guarini cases were originally filed seeking damages relating to the government's elimination of certain tax deductions. Seven of those eight cases have now concluded. One case settled in 2002 for \$20,000, and a second case concluded in 2004 with no damage award. Judgments were paid in four cases in 2005 and 2006 for a total of \$152.6 million. In a seventh case settled in 2006 for \$99 million, the settlement agreement further obligates the FRF-FSLIC as a

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guarantor for all tax liabilities in the event the settlement amount is determined by tax authorities to be taxable. The maximum potential exposure under this guarantee through 2009 is approximately \$81 million. After reviewing relevant case law in relation to the nature of the settlement, the FDIC believes that it is very unlikely the settlement will be subject to taxation. Therefore, the FRF is not expected to fund any payment under this guarantee and no liability has been recorded. The eighth Guarini case is currently before the U.S. Court of Federal Claims for consideration of one remaining issue.

The FDIC has established a contingent liability of approximately \$27.5 million for the remaining Guarini litigation loss exposure.

#### **Representations and Warranties**

As part of the RTC's efforts to maximize the return from the sale of assets from thrift resolutions, representations and warranties, and guarantees were offered on certain loan sales. The majority of loans subject to these agreements have been paid off, refinanced, or the period for filing claims has expired. The FDIC's estimate of maximum potential exposure to the FRF is \$30 million based on an assessment of remaining portfolio balances still covered by representations and warranties. No claims in connection with representations and warranties have been asserted since 1998 on the remaining open agreements. Because of the age of the remaining portfolio and lack of claim activity, the FDIC does not expect new claims to be asserted in the future. Consequently, the financial statements at December 31, 2006 and 2005 do not include a liability for these agreements.

## FSLIC Resolution Fund

### 5. Resolution Equity

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

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

#### Resolution Equity at December 31, 2006

Dollars in Thousands

	FRF-FSLIC	FRF-RTC	FRF Consolidated
Contributed capital - beginning	\$ 44,808,104	\$ 82,199,337	\$ 127,007,441
Add: U.S. Treasury payments for goodwill litigation	446,555	0	446,555
<b>Contributed capital - ending</b>	<b>45,254,659</b>	<b>82,199,337</b>	<b>127,453,996</b>
Accumulated deficit	(42,212,338)	(81,621,459)	(123,833,797)
<b>Total</b>	<b>\$ 3,042,321</b>	<b>\$ 577,878</b>	<b>\$ 3,620,199</b>

#### Contributed Capital

The FRF-FSLIC and the former RTC received \$43.5 billion and \$60.1 billion from the U.S. Treasury, respectively, to fund losses from thrift resolutions prior to July 1, 1995. Additionally, the FRF-FSLIC issued \$670 million in capital certificates to the Financing Corporation (a mixed-ownership government corporation established to function solely as a financing vehicle for the FSLIC) and the RTC issued \$31.3 billion of these instruments to the REFCORP. FIRREA prohibited the payment of dividends on any of these capital certificates. Through December 31, 2006, the FRF-RTC has returned \$4.556 billion to the U.S. Treasury and made payments of \$4.572 billion to the REFCORP. These actions serve to reduce contributed capital.

During 2006, the FRF-FSLIC received \$194.7 million for U.S. Treasury payments for goodwill litigation and established a receivable for \$251.8 million (see Note 4).

#### Accumulated Deficit

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



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## 6. Employee Benefits

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### **Pension Benefits**

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Eligible FDIC employees (permanent and term employees with appointments exceeding one year) are covered by the federal government retirement plans, either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). Although the FRF contributes a portion of pension benefits for eligible employees, it does not account for the assets of either retirement system. The FRF also does not have actuarial data for accumulated plan benefits or the unfunded liability relative to eligible employees. These amounts are reported on and accounted for by the U.S. Office of Personnel Management. The FRF's pension-related expenses were \$850 thousand and \$2.9 million for 2006 and 2005, respectively.

### **Postretirement Benefits Other Than Pensions**

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The FRF no longer records a liability for the postretirement benefits of life and dental insurance as a result of FDIC's change in funding policy for these benefits and elimination of the separate entity formerly used to account for such estimated future costs. In implementing this change, management decided not to allocate either the plan assets or the revised net accumulated postretirement benefit obligation (a long-term liability) to the FRF due to the expected dissolution of the FRF. However, the FRF does continue to pay its proportionate share of the yearly claim expenses associated with these benefits.



United States Government Accountability Office  
Washington, D.C. 20548

To the Board of Directors  
The Federal Deposit Insurance Corporation

We have audited the balance sheets as of December 31, 2006, and 2005, for the two funds administered by the Federal Deposit Insurance Corporation (FDIC), the related statements of income and fund balance (accumulated deficit), and the statements of cash flows for the years then ended. In our audits of the Deposit Insurance Fund (DIF) and the FSLIC Resolution Fund (FRF), we found

- the financial statements of each fund are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles;
- FDIC had effective internal control over financial reporting and compliance with laws and regulations for each fund; and
- no reportable noncompliance with laws and regulations we tested.

The following sections discuss our conclusions in more detail. They also present information on the scope of our audits and our evaluation of FDIC management's comments on a draft of this report.

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## Opinion on DIF's Financial Statements

The financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, DIF's financial position as of December 31, 2006, and 2005, and the results of its operations and its cash flows for the years then ended.

As discussed in note 1 to DIF's financial statements, on February 8, 2006, the President signed into law the Federal Deposit Insurance Reform Act of 2005 (the Act). Among its provisions, the Act called for the merger of the Bank Insurance Fund (BIF) and Savings Association Insurance Fund (SAIF) into a single deposit insurance fund. In accordance with the Act, on March 31, 2006, FDIC established the DIF with the merger of the BIF and SAIF. As further discussed in note 2 to DIF's financial statements, the merger resulted in a new reporting entity. The financial results of the newly formed DIF were retrospectively applied as though they had been combined at the beginning of the reporting year as well as for prior periods presented for comparative purposes.

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## Opinion on FRF's Financial Statements

The financial statements, including the accompanying notes, present fairly, in all material respects, in conformity with U.S. generally accepted accounting principles, FRF's financial position as of December 31, 2006, and 2005, and the results of its operations and its cash flows for the years then ended.

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## Opinion on Internal Control

FDIC management maintained, in all material respects, effective internal control over financial reporting (including safeguarding assets) and compliance as of December 31, 2006, that provided reasonable assurance that misstatements, losses, or noncompliance material in relation to FDIC's financial statements for each fund would be prevented or detected on a timely basis. Our opinion is based on criteria established under 31 U.S.C. 3512 (c), (d) [commonly known as the Federal Managers' Financial Integrity Act (FMFIA)].

In our prior year audit,<sup>1</sup> we reported on weaknesses we identified in FDIC's information system controls, which we considered to be a reportable condition.<sup>2</sup> Specifically, FDIC had implemented a new financial system May 2005 and, in doing so, did not ensure that controls were adequate to accommodate its new systems environment.

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<sup>1</sup> GAO, *Financial Audit: Federal Deposit Insurance Corporation Funds' 2005 and 2004 Financial Statements*, GAO-06-146 (Washington, D.C.: Mar. 2, 2006).

<sup>2</sup> Reportable conditions involve matters coming to the auditor's attention that, in the auditor's judgment, should be communicated because they represent significant deficiencies in the design or operation of internal control and could adversely affect FDIC's ability to meet the control objectives described in this report. In May 2006, the American Institute of Certified Public Accountants (AICPA) issued Statement on Auditing Standard (SAS) 112, which became effective for audits of financial statements for periods ending on or after December 15, 2006. SAS 112 established standards and provides guidance on the auditor's responsibilities for identifying, evaluating, and communicating matters related to an entity's internal control over financial reporting identified in an audit of financial statements. Under the new SAS, the auditor is required to communicate control deficiencies that are significant deficiencies or material weaknesses in internal controls. A significant deficiency is a control deficiency, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. As a result of SAS 112, the term reportable condition is no longer used.

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During 2006, FDIC corrected many of these weaknesses and implemented mitigating or compensating controls to provide protection for the corporation's financial and sensitive information in the new systems environment. These improvements enabled us to conclude that the remaining issues related to information systems controls do not constitute a significant deficiency. However, continued management commitment to an effective information security program will be essential to ensure that the corporation's financial and sensitive information will be adequately protected. In light of the evolving nature of information security, and with new exposures and threats continuing to develop, the corporation's information security program will need to dynamically adapt to address changing information security challenges. As FDIC continues to enhance its new financial system, which is based on an integrated financial management software package, the corporation's reliance on controls implemented in the single, integrated financial system will increase. The continued effectiveness of FDIC's controls will be dependent on sound implementation of the integrated financial management software and its operations.

We did identify control deficiencies during our 2006 audits that we do not consider to be significant deficiencies. We will be reporting separately to FDIC management on these matters.

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## Compliance with Laws and Regulations

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

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## Objectives, Scope, and Methodology

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

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

- financial reporting—transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in conformity with U.S. generally accepted accounting principles; and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and

- 
- compliance with laws and regulations—transactions are executed in accordance with laws and regulations that could have a direct and material effect on the financial statements.

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

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- assessed the accounting principles used and significant estimates made by management;
- evaluated the overall presentation of the financial statements;
- obtained an understanding of internal control related to financial reporting (including safeguarding assets) and compliance with laws and regulations;
- tested relevant internal controls over financial reporting and compliance, and evaluated the design and operating effectiveness of internal control;
- considered FDIC's process for evaluating and reporting on internal control based on criteria established by FMFIA; and
- tested compliance with certain laws and regulations, including selected provisions of the Federal Deposit Insurance Act, as amended, the Federal Deposit Insurance Reform Act of 2005, and the Chief Financial Officers Act of 1990.

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

We did not test compliance with all laws and regulations applicable to FDIC. We limited our tests of compliance to those laws and regulations that could have a direct and material effect on the financial statements for the year ended December 31, 2006. We caution that noncompliance may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

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

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## FDIC Comments and Our Evaluation

In commenting on a draft of this report, FDIC's Chief Financial Officer (CFO) was pleased to receive unqualified opinions on the DIF and FRF financial statements and to note that there were no material weaknesses identified during the 2006 audits. FDIC's CFO appreciated that we recognized the improvements that FDIC made over the past year to its information systems environment. Also, the CFO stated that FDIC's sustained commitment to enhancing information systems controls adequately addressed the concerns that we highlighted in the prior year report and enabled us to conclude that the remaining issues related to such controls do not constitute a significant deficiency. Finally, the CFO stated that FDIC's goal is to maintain an effective information security program going forward, and has pledged to work diligently to resolve control issues that we identified during the 2006 audits, as well as any that may arise in the future.

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



David M. Walker  
Comptroller General  
of the United States

January 31, 2007



**Federal Deposit Insurance Corporation**  
550 17th Street, NW Washington, DC 20429

Deputy to the Chairman and Chief Financial Officer

February 8, 2007

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

**Re: FDIC Management Response on the GAO 2006 Financial Statements Audit Report**

Dear Mr. Walker:

Thank you for the opportunity to comment on the U.S. Government Accountability Office's (GAO) draft audit report titled, **Financial Audit: Federal Deposit Insurance Corporation Funds' 2006 and 2005 Financial Statements, GAO-07-371**. The report presents GAO's opinions on the calendar year 2006 and 2005 financial statements of the Deposit Insurance Fund (DIF) and the Federal Savings and Loan Insurance Corporation Resolution Fund (FRF). The report also presents GAO's opinion on the effectiveness of FDIC's internal controls as of December 31, 2006, and GAO's evaluation of FDIC's compliance with selected laws and regulations.

We are pleased to accept GAO's unqualified opinions on the DIF and the FRF financial statements and to note that there were no material weaknesses identified during the 2006 audits. The GAO reported that the funds' financial statements were presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles; FDIC had effective internal control over financial reporting and compliance with laws and regulations for each fund; and there were no instances of noncompliance with laws and regulations that were tested.

In addition, we appreciate that GAO recognized the improvements that FDIC made over the past year to its information systems environment. We believe that our sustained commitment to enhancing information systems controls adequately addressed the concerns that GAO highlighted in the prior year report, thus enabling GAO to conclude that the remaining issues related to such controls do not constitute a significant deficiency. Our goal is to maintain an effective information security program going forward. Accordingly, we will work diligently to resolve any control issues that GAO identified during its 2006 audits, as well as any that may arise in the future.

We look forward to continuing our cooperative working relationship with the GAO in the coming year. Our collaborative efforts and open communication at all levels of our organizations should ensure continued success. If you have any questions or concerns, please do not hesitate to contact me.

Sincerely,

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

## Overview of the Industry

The 8,743 FDIC-insured commercial banks and savings institutions that filed financial results for the first three quarters of 2006 reported year-to-date net income of \$112.4 billion (excludes 12 U.S. branches of foreign banks). This was \$10.6 billion (10.4 percent) more than the industry reported for the first three quarters of 2005, and represented the largest three-quarter earnings total ever reported by the industry. The improvement in earnings reflected strong growth in loans and other interest-bearing investments, very good asset quality, and higher noninterest income at larger institutions. More than half of all insured institutions—56.8 percent—reported earnings increases for the first three quarters of 2006, but the percentage of institutions that were unprofitable increased to 6.9 percent, from 5.8 percent in the first three quarters of 2005.

Profitability, as measured by return on assets (ROA), remained very high by historic standards. For the first three quarters of 2006, the industry ROA was 1.33 percent, the same as in the first three quarters of 2005, and the third-highest ever registered for a nine-month period. Earnings growth was led by increased noninterest income. Total noninterest

income grew by \$17.6 billion (10.5 percent) compared to the same period in 2005. Income from trading was \$3.9 billion (34.6 percent) higher than a year earlier, securitization income was \$2.5 billion (14.1 percent) higher, and income from investment banking increased by \$1.6 billion (20.8 percent). Net interest income was \$16.0 billion higher than in the same period of 2005, but this represented only a 6.7 percent increase, while interest-earning assets grew by 9.7 percent. The relatively sluggish growth in net interest income reflected narrower net interest margins caused by rising short-term interest rates and a flattening yield curve. Improvements in asset quality also provided a boost to earnings in 2006. Provisions for loan and lease losses were \$1.8 billion (8.1 percent) lower than in 2005, as net charge-offs declined by \$3.6 billion (16.0 percent). Lower gains on sales of securities and other assets (down \$2.5 billion, or 58.3 percent), and higher noninterest expenses (up \$18.0 billion, or 7.6 percent) limited the improvement in earnings.

Asset growth at insured institutions remained very robust in 2006. For the 12 months ended September 30, 2006, total assets of FDIC-insured institutions grew by \$1.1 trillion (9.9 percent). Loans and leases accounted for more than half of the growth in assets (56.2 percent), while growth in securities accounted for almost one-tenth of the increase in total assets (9.6 percent). Loans

to commercial borrowers accounted for two-thirds of the growth in total loans, with loans to commercial and industrial (C&I) borrowers, real estate construction and development loans, and loans secured by nonfarm non-residential properties registering the biggest increases. Residential mortgage loans had the largest increase of any single loan category, growing by \$158 billion (7.8 percent).

Deposit growth was also strong in 2006, but it did not keep pace with the rapid growth in assets. Total deposits increased by \$609.5 billion (8.7 percent) between September 30, 2005, and September 30, 2006, but this growth represented only 57.7 percent of insured institutions' funding needs. Nondeposit liabilities increased by \$315 billion (12.0 percent) during this period, and equity capital grew by \$132.5 billion (12.1 percent). Merger-related goodwill accounted for almost one-third (\$43.1 billion, or 32.6 percent) of the total increase in equity capital. More than 99 percent of all insured institutions met or exceeded the highest regulatory capital requirements as of September 30.



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Asset quality indicators remained very positive in 2006. At mid-year, the percentage of loans and leases that were noncurrent (90 days or more past due or in nonaccrual status) reached the lowest level in the 23 years that all insured institutions have reported noncurrent loan data. The industry's net charge-off rate was also at a historical low level in 2006. At the end of the third quarter, the number of institutions on the FDIC's "Problem List" stood at 47, the lowest level in the 36 years for which data are available.

## V. Management Control

### Enterprise Risk Management

The Office of Enterprise Risk Management, under the auspices of the Chief Financial Officer organization, is responsible for corporate oversight of internal control and enterprise risk management (ERM). This includes ensuring that the FDIC's operations and programs are effective and efficient and that internal controls are sufficient to minimize exposure to waste and mismanagement. The FDIC recognizes the importance of a strong risk management and internal control program and has adopted a more proactive and enterprise-wide approach to managing risk. This approach focuses on the identification and mitigation of risk consistently and effectively throughout the Corporation, with emphasis on those areas/issues most directly related to our overall missions. As an independent government corporation, the FDIC has different requirements than the mainstream federal government; nevertheless, its ERM program seeks to comply with the spirit of the following standards, among others:

- Federal Managers' Financial Integrity Act (FMFIA);
- Chief Financial Officers Act (CFO Act);
- Government Performance and Results Act (GPRA);
- Federal Information Security Management Act (FISMA); and
- OMB Circular A-123.

The CFO Act extends to the FDIC the FMFIA requirements for establishing, evaluating and reporting on internal controls. The FMFIA requires agencies to annually provide a statement of assurance regarding the effectiveness of management, administrative and accounting controls, and financial management systems.

The FDIC has developed and implemented management, administrative and financial system controls that reasonably ensure that:

- Programs are efficiently and effectively carried out in accordance with applicable laws and management policies;
- Programs and resources are safeguarded against waste, fraud and mismanagement;
- Obligations and costs comply with applicable laws; and
- Reliable, complete, and timely data are maintained for decision-making and reporting purposes.

The FDIC's control standards incorporate the *Government Accountability Office's (GAO) Standards for Internal Control in the Federal Government*. Good internal control systems are essential for ensuring the proper conduct of FDIC business and the accomplishment of management objectives by serving as checks and balances against undesirable actions or outcomes.

As part of the Corporation's continued commitment to establish and maintain effective and efficient internal controls, FDIC management routinely conducts reviews of internal control systems. The results of these reviews, as well as consideration of the results of audits, evaluations and reviews conducted by the GAO, the Office of Inspector General (OIG) and other outside entities, are used as a basis for the FDIC's reporting on the condition of the Corporation's internal control activities.

### Material Weaknesses

Material weaknesses are control shortcomings in operations or systems that, among other things, severely impair or threaten the organization's ability to accomplish its mission or to prepare timely, accurate financial statements or reports. The shortcomings are of sufficient magnitude that the Corporation is obliged to report them to external stakeholders.

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To determine the existence of material weaknesses, the FDIC has assessed the results of management evaluations and external audits of the Corporation's risk management and internal control systems conducted in 2006, as well as management actions taken to address issues identified in these audits and evaluations. Based on this assessment and application of other criteria, the FDIC concludes that no material weaknesses existed within the Corporation's operations for 2006. This is the ninth consecutive year that the FDIC has not had a material weakness; however, FDIC management will continue to focus on high priority areas, including various aspects of deposit insurance reform, IT systems security, contract acquisition management, the New Financial Environment, emergency response plan, privacy, and records management, among others. The FDIC will also address all control issues raised by GAO related to its 2006 financial statement audit report.

### **Management Report on Final Actions**

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As required under amended Section 5 of the Inspector General Act of 1978, the tables on the following pages provide information on final action taken by management on audit reports for the federal fiscal year period, October 1, 2005, through September 30, 2006.

Table 1  
**Management Report  
on Final Action on Audits  
with Disallowed Costs**  
For Fiscal Year 2006  
(October 1, 2005-September 30, 2006)

<b>Audit Reports</b>	<b>Number of Reports</b>	<b>Disallowed Costs (000's)</b>
A. Management decisions – final action not taken at beginning of period	2	\$ 1,969
B. Management decisions made during the period	1	\$ 46
C. Total reports pending final action during the period (A and B)	3	\$ 2,015
D. Audit reports on which final action was taken during the period:		
1. Recoveries:		
a. Collections and offsets	3	\$ 36
b. Other	0	\$ 0
2. Write-offs	2	\$ 1,982
3. Total of 1(a), 1(b), and 2	3 <sup>•</sup>	\$ 2,018 <sup>▲</sup>
E. Audit reports needing final action at the end of the period	0	\$ 0

• Two reports have both collections and write-offs, thus the total of 1(a), 1(b), and 2 is three.

▲ Collections for one report in line D1(a) was more than the amount disallowed in line B for that report; thus line D3 exceeds line C.

Table 2  
**Management Report  
on Final Action on Audits  
with Recommendations  
to Put Funds to Better Use**  
For Fiscal Year 2006  
(October 1, 2005-September 30, 2006)

<b>Audit Reports</b>	<b>Number of Reports</b>	<b>Funds Put to Better Use (000's)</b>
A. Management decisions – final action not taken at beginning of period	0	\$ 0
B. Management decisions made during the period	0	\$ 0
C. Total reports pending final action during the period (A and B)	0	\$ 0
D. Final Action taken during the period:		
1. Value of recommendations implemented (completed)	0	\$ 0
2. Value of recommendations that management concluded should not or could not be implemented or completed	0	\$ 0
3. Total of 1 and 2	0	\$ 0
E. Audit reports needing final action at the end of the period	0	\$ 0

Table 3

**Audit Reports Without Final Actions But With Management Decisions Over One Year Old**

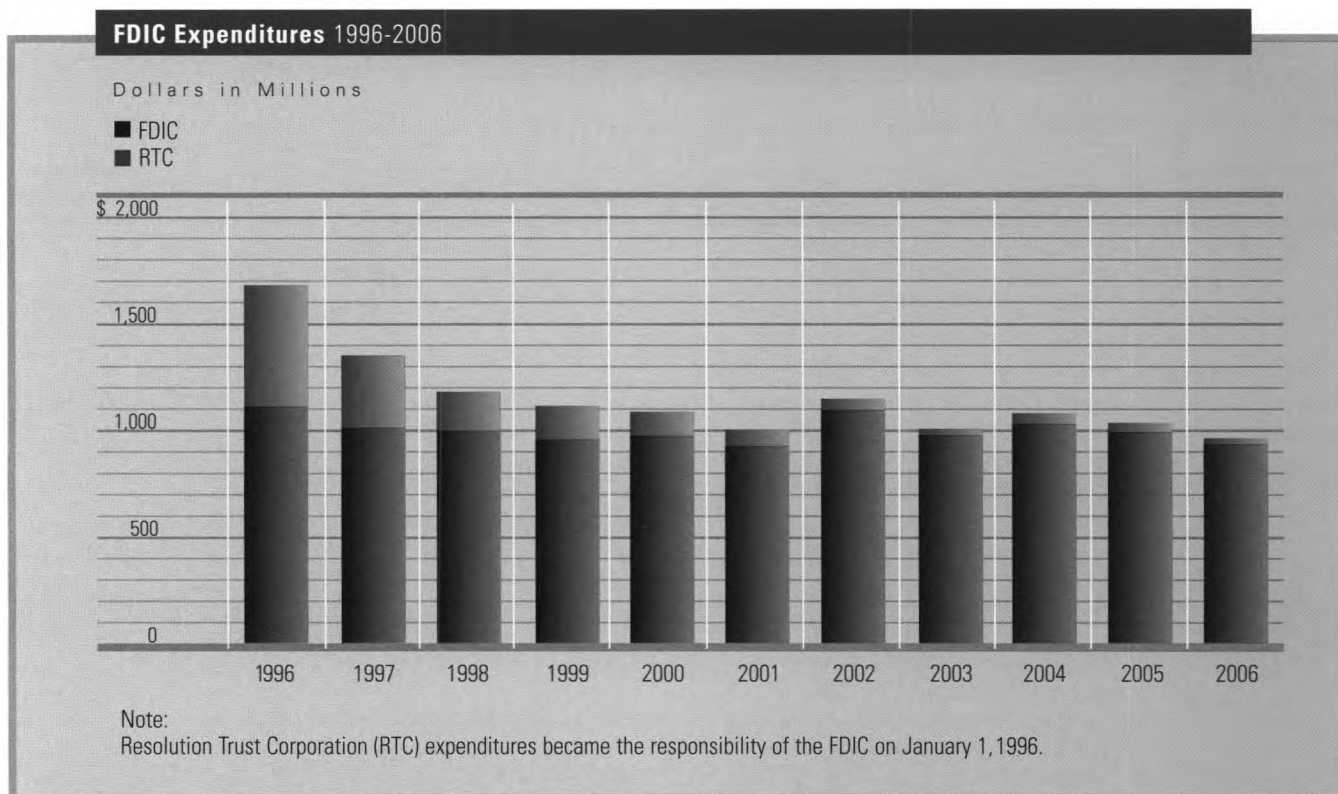
For Fiscal Year 2006 (October 1, 2005-September 30, 2006)

**Management Action in Process**

<b>Report Number and Issue Date</b>	<b>OIG Audit Finding</b>	<b>Management Action</b>	<b>Disallowed Costs</b>
1. <b>03-007</b> 11-27-02	The OIG made recommendations for improvements in the FDIC's internal network controls.	FDIC is working to secure sensitive data in conjunction with implementation of the enterprise encryption project.  Expected completion date: 1st quarter 2007.	\$ 0
2. <b>04-019</b> 04-30-04	The OIG identified best practices that should be associated with the System Development Life Cycle methodology and related control framework that will be adopted by the Corporation.	Management is in the process of reviewing closure documentation.  Expected completion date: 1st quarter 2007.	\$ 0
3. <b>05-031</b> 09-08-05	The OIG made recommendations to establish an organizational policy and system-specific procedures to ensure proper configuration management of operating system software.	Management is in the process of reviewing closure documentation.  Expected completion date: 1st quarter 2007.	\$ 0
4. <b>05-036</b> 09-21-05	The OIG made a recommendation to research the General Services Administration's (GSA's) e-Travel Programs and determine whether the travel services available under the programs could improve or replace the FDIC's current travel program.	Management is in the process of reviewing the benefits of each of GSA's e-Travel programs. Additionally, management will review other commercial travel processing systems along with FDIC's travel system to determine the feasibility of adding capabilities available in GSA's programs.  Expected completion date: 3rd quarter 2007.	\$ 0

## VI. Appendices

### Appendix A – Key Statistics



The FDIC's Strategic Plan and Annual Performance Plan provide the basis for annual planning and budgeting for needed resources. The 2006 aggregate budget (for corporate, receivership and investment spending) was \$1.09 billion, while actual expenditures for the year were \$1.00 billion, about \$55 million less than 2005 expenditures.

Over the past ten years, the FDIC's expenditures have varied in response to workload. During the past decade, expenditures generally declined due to decreasing resolution and receivership activity. Total expenditures increased in 2002 due to an increase in receivership-related expenses.

The largest component of FDIC spending is for costs associated with staffing. Staffing decreased by 1 percent in 2006, from 4,514 employees at the beginning of the year to 4,476 at the end of the year.

## Estimated Insured Deposits and the Deposit Insurance Fund, December 31, 1934, through September 30, 2006<sup>1</sup>

Dollars in millions							
Year	Insurance Coverage	Deposits in Insured Institutions			Insurance Fund as a Percentage of		
		Total Domestic Deposits	Estimated Insured Deposits <sup>2</sup>	Percentage of Insured Deposits	Deposit Insurance Fund	Total Domestic Deposits	Estimated Insured Deposits
<b>2006</b>	<b>\$ 100,000</b>	<b>\$ 6,439,416</b>	<b>\$ 4,094,765</b>	<b>63.6</b>	<b>\$ 49,991.9</b>	<b>0.78</b>	<b>1.22</b>
2005	100,000	6,168,146	3,890,911	63.1	48,596.6	0.79	1.25
2004	100,000	5,686,680	3,623,713	63.7	47,506.8	0.84	1.31
2003	100,000	5,182,016	3,451,117	66.6	46,022.3	0.89	1.33
2002	100,000	4,857,327	3,387,799	69.7	43,797.0	0.90	1.29
2001	100,000	4,481,888	3,210,727	71.6	41,373.8	0.92	1.29
2000	100,000	4,149,355	3,054,360	73.6	41,733.8	1.01	1.37
1999	100,000	3,802,744	2,868,881	75.4	39,694.9	1.04	1.38
1998	100,000	3,747,809	2,850,227	76.1	39,452.1	1.05	1.38
1997	100,000	3,507,493	2,746,006	78.3	37,660.8	1.07	1.37
1996	100,000	3,350,856	2,690,537	80.3	35,742.8	1.07	1.33
1995	100,000	3,318,513	2,663,560	80.3	28,811.5	0.87	1.08
1994	100,000	3,184,636	2,588,686	81.3	23,784.5	0.75	0.92
1993	100,000	3,220,109	2,602,043	80.8	14,277.3	0.44	0.55
1992	100,000	3,273,180	2,675,081	81.7	178.4	0.01	0.01
1991	100,000	3,330,738	2,734,073	82.1	(6,934.0)	(0.21)	(0.25)
1990	100,000	3,415,668	2,759,640	80.8	4,062.7	0.12	0.15
1989	100,000	3,414,066	2,756,757	80.7	13,209.5	0.39	0.48
1988	100,000	2,330,768	1,750,259	75.1	14,061.1	0.60	0.80
1987	100,000	2,201,549	1,658,802	75.3	18,301.8	0.83	1.10
1986	100,000	2,167,596	1,634,302	75.4	18,253.3	0.84	1.12
1985	100,000	1,974,512	1,503,393	76.1	17,956.9	0.91	1.19
1984	100,000	1,806,520	1,389,874	76.9	16,529.4	0.92	1.19
1983	100,000	1,690,576	1,268,332	75.0	15,429.1	0.91	1.22
1982	100,000	1,544,697	1,134,221	73.4	13,770.9	0.89	1.21
1981	100,000	1,409,322	988,898	70.2	12,246.1	0.87	1.24
1980	100,000	1,324,463	948,717	71.6	11,019.5	0.83	1.16
1979	40,000	1,226,943	808,555	65.9	9,792.7	0.80	1.21
1978	40,000	1,145,835	760,706	66.4	8,796.0	0.77	1.16
1977	40,000	1,050,435	692,533	65.9	7,992.8	0.76	1.15
1976	40,000	941,923	628,263	66.7	7,268.8	0.77	1.16
1975	40,000	875,985	569,101	65.0	6,716.0	0.77	1.18
1974	40,000	833,277	520,309	62.5	6,124.2	0.73	1.18
1973	20,000	766,509	465,600	60.7	5,615.3	0.73	1.21
1972	20,000	697,480	419,756	60.2	5,158.7	0.74	1.23
1971	20,000	610,685	374,568	61.3	4,739.9	0.78	1.27
1970	20,000	545,198	349,581	64.1	4,379.6	0.80	1.25
1969	20,000	495,858	313,085	63.1	4,051.1	0.82	1.29
1968	15,000	491,513	296,701	60.2	3,749.2	0.76	1.26
1967	15,000	448,709	261,149	58.2	3,485.5	0.78	1.33
1966	15,000	401,096	234,150	58.4	3,252.0	0.81	1.39
1965	10,000	377,400	209,690	55.6	3,036.3	0.80	1.45
1964	10,000	348,981	191,787	55.0	2,844.7	0.82	1.48
1963	10,000	313,304	177,381	56.6	2,667.9	0.85	1.50
1962	10,000	297,548	170,210	57.2	2,502.0	0.84	1.47
1961	10,000	281,304	160,309	57.0	2,353.8	0.84	1.47
1960	10,000	260,495	149,684	57.5	2,222.2	0.85	1.48
1959	10,000	247,589	142,131	57.4	2,089.8	0.84	1.47
1958	10,000	242,445	137,698	56.8	1,965.4	0.81	1.43
1957	10,000	225,507	127,055	56.3	1,850.5	0.82	1.46
1956	10,000	219,393	121,008	55.2	1,742.1	0.79	1.44
1955	10,000	212,226	116,380	54.8	1,639.6	0.77	1.41
1954	10,000	203,195	110,973	54.6	1,542.7	0.76	1.39
1953	10,000	193,466	105,610	54.6	1,450.7	0.75	1.37
1952	10,000	188,142	101,841	54.1	1,363.5	0.72	1.34
1951	10,000	178,540	96,713	54.2	1,282.2	0.72	1.33
1950	10,000	167,818	91,359	54.4	1,243.9	0.74	1.36
1949	5,000	156,786	76,589	48.8	1,203.9	0.77	1.57
1948	5,000	153,454	75,320	49.1	1,065.9	0.69	1.42
1947	5,000	154,096	76,254	49.5	1,006.1	0.65	1.32
1946	5,000	148,458	73,759	49.7	1,058.5	0.71	1.44
1945	5,000	157,174	67,021	42.4	929.2	0.59	1.39
1944	5,000	134,662	56,398	41.9	804.3	0.60	1.43
1943	5,000	111,650	48,440	43.4	703.1	0.63	1.45
1942	5,000	89,869	32,837	36.5	616.9	0.69	1.88
1941	5,000	71,209	28,249	39.7	553.5	0.78	1.96
1940	5,000	65,288	26,638	40.8	496.0	0.76	1.86
1939	5,000	57,485	24,650	42.9	452.7	0.79	1.84
1938	5,000	50,791	23,121	45.5	420.5	0.83	1.82
1937	5,000	48,228	22,557	46.8	383.1	0.79	1.70
1936	5,000	50,281	22,330	44.4	343.4	0.68	1.54
1935	5,000	45,125	20,158	44.7	306.0	0.68	1.52
1934 <sup>3</sup>	5,000	40,060	18,075	45.1	291.7	0.73	1.61

<sup>1</sup> For 2006, the numbers are as of September 30, and prior years reflect December 31.

<sup>2</sup> Estimated insured deposits reflect deposit information as reported in the fourth quarter *FDIC Quarterly Banking Profile*. Before 1991, insured deposits were estimated using percentages determined from the June 30 *Call Reports*.

<sup>3</sup> Initial coverage was \$2,500 from January 1 to June 30, 1934.

**Income and Expenses, Deposit Insurance Fund, from Beginning of Operations,  
September 11, 1933, through December 31, 2006**

Dollars in Millions

Year	Income					Expenses and Losses					Net Income/ (Loss)
	Total	Assessment Income	Assessment Credits	Investment and Other Sources	Effective Assessment Rate <sup>1</sup>	Total	Provision for Losses	Administrative and Operating Expenses <sup>2</sup>	Interest and Other Insurance Expenses	Funding Transfer from the FSLIC Resolution Fund	
<b>Total</b>	<b>\$ 107,192.5</b>	<b>\$ 62,266.9</b>	<b>\$ 6,709.1</b>	<b>\$ 52,223.7</b>		<b>\$ 58,125.1</b>	<b>\$ 36,096.8</b>	<b>\$ 14,841.7</b>	<b>\$ 7,192.6</b>	<b>\$139.5</b>	<b>\$ 49,206.9</b>
2006	2,643.5	31.9	0.0	2,611.6	0.0005%	904.3	(52.1)	950.6	5.8	0	1,739.2
2005	2,420.5	60.6	0.0	2,359.9	0.0010%	809.5	(160.2)	966.2	3.5	0	1,611.0
2004	2,240.4	104.3	0.0	2,136.1	0.0019%	607.6	(353.4)	941.3	19.7	0	1,632.8
2003	2,174.0	95.2	0.0	2,078.8	0.0019%	(67.7)	(1,010.5)	935.5	7.3	0	2,241.7
2002	1,795.9	108.0	0.0	2,276.9	0.0022%	719.6	(243.0)	945.1	17.5	0	1,076.3
2001	2,729.7	82.8	0.0	2,646.9	0.0019%	3,123.4	2,199.3	887.9	36.2	0	(393.7)
2000	2,569.9	64.1	0.0	2,505.8	0.0016%	945.2	28.0	883.9	33.3	0	1,624.7
1999	2,416.6	48.3	0.0	2,368.3	0.0013%	2,047.0	1,199.7	823.4	23.9	0	369.6
1998	2,584.3	36.7	0.0	2,547.6	0.0010%	817.5	(5.7)	782.6	40.6	0	1,766.8
1997	2,165.6	38.7	0.0	2,126.9	0.0015%	247.3	(505.7)	677.2	75.8	0	1,918.3
1996	7,157.3	5,294.7	0.0	1,862.6	0.1627%	353.6	(417.2)	568.3	202.5	0	6,803.7
1995	5,229.1	3,876.9	0.0	1,352.2	0.1242%	202.2	(354.2)	510.6	45.8	0	5,026.9
1994	7,682.0	6,722.6	0.0	959.4	0.2185%	(1,825.1)	(2,459.4)	443.2	191.1	0	9,507.1
1993	7,356.8	6,684.3	0.0	672.5	0.2146%	(6,744.4)	(7,660.4)	418.5	497.5	0	14,101.2
1992	6,480.5	5,759.8	0.0	720.7	0.1807%	(596.8)	(2,274.7)	614.8 <sup>3</sup>	1,063.1	35.4	7,112.7
1991	5,887.0	5,254.5	0.0	632.5	0.1605%	16,925.3	15,496.2	326.1	1,103.0	42.4	(10,995.9)
1990	3,856.3	2,873.3	0.0	983.0	0.0867%	13,059.3	12,133.1	275.6	650.6	56.1	(9,146.9)
1989	3,496.6	1,885.0	0.0	1,611.6	0.0001%	4,352.2	3,811.3	219.9	321.0	5.6	(850.0)
1988	3,347.7	1,773.0	0.0	1,574.7	0.0833%	7,588.4	6,298.3	223.9	1,066.2	0	(4,240.7)
1987	3,319.4	1,696.0	0.0	1,623.4	0.0833%	3,270.9	2,996.9	204.9	69.1	0	48.5
1986	3,260.1	1,516.9	0.0	1,743.2	0.0833%	2,963.7	2,827.7	180.3	(44.3)	0	296.4
1985	3,385.4	1,433.4	0.0	1,952.0	0.0833%	1,957.9	1,569.0	179.2	209.7	0	1,427.5
1984	3,099.5	1,321.5	0.0	1,778.0	0.0800%	1,999.2	1,633.4	151.2	214.6	0	1,100.3
1983	2,628.1	1,214.9	164.0	1,577.2	0.0714%	969.9	675.1	135.7	159.1	0	1,658.2
1982	2,524.6	1,108.9	96.2	1,511.9	0.0769%	999.8	126.4	129.9	743.5	0	1,524.8
1981	2,074.7	1,039.0	117.1	1,152.8	0.0714%	848.1	320.4	127.2	400.5	0	1,226.6
1980	1,310.4	951.9	521.1	879.6	0.0370%	83.6	(38.1)	118.2	3.5	0	1,226.8
1979	1,090.4	881.0	524.6	734.0	0.0333%	93.7	(17.2)	106.8	4.1	0	996.7
1978	952.1	810.1	443.1	585.1	0.0385%	148.9	36.5	103.3	9.1	0	803.2
1977	837.8	731.3	411.9	518.4	0.0370%	113.6	20.8	89.3	3.5	0	724.2
1976	764.9	676.1	379.6	468.4	0.0370%	212.3	28.0	180.4 <sup>4</sup>	3.9	0	552.6
1975	689.3	641.3	362.4	410.4	0.0357%	97.5	27.6	67.7	2.2	0	591.8
1974	668.1	587.4	285.4	366.1	0.0435%	159.2	97.9	59.2	2.1	0	508.9
1973	561.0	529.4	283.4	315.0	0.0385%	108.2	52.5	54.4	1.3	0	452.8
1972	467.0	468.8	280.3	278.5	0.0333%	59.7	10.1	49.6	6.0 <sup>5</sup>	0	407.3
1971	415.3	417.2	241.4	239.5	0.0345%	60.3	13.4	46.9	0.0	0	355.0
1970	382.7	369.3	210.0	223.4	0.0357%	46.0	3.8	42.2	0.0	0	336.7
1969	335.8	364.2	220.2	191.8	0.0333%	34.5	1.0	33.5	0.0	0	301.3
1968	295.0	334.5	202.1	162.6	0.0333%	29.1	0.1	29.0	0.0	0	265.9
1967	263.0	303.1	182.4	142.3	0.0333%	27.3	2.9	24.4	0.0	0	235.7
1966	241.0	284.3	172.6	129.3	0.0323%	19.9	0.1	19.8	0.0	0	221.1
1965	214.6	260.5	158.3	112.4	0.0323%	22.9	5.2	17.7	0.0	0	191.7
1964	197.1	238.2	145.2	104.1	0.0323%	18.4	2.9	15.5	0.0	0	178.7
1963	181.9	220.6	136.4	97.7	0.0313%	15.1	0.7	14.4	0.0	0	166.8
1962	161.1	203.4	126.9	84.6	0.0313%	13.8	0.1	13.7	0.0	0	147.3

continued on next page





**Income and Expenses, Deposit Insurance Fund, from Beginning of Operations, September 11, 1933, through December 31, 2006** (continued)

Dollars in Millions

Year	Income					Expenses and Losses						Net Income/ (Loss)
	Total	Assessment Income	Assessment Credits	Investment and Other Sources	Effective Assessment Rate <sup>1</sup>	Total	Provision for Losses	Administrative and Operating Expenses <sup>2</sup>	Interest and Other Insurance Expenses	Funding Transfer from the FSLIC Resolution Fund		
1961	147.3	188.9	115.5	73.9	0.0323%	14.8	1.6	13.2	0.0	0	132.5	
1960	144.6	180.4	100.8	65.0	0.0370%	12.5	0.1	12.4	0.0	0	132.1	
1959	136.5	178.2	99.6	57.9	0.0370%	12.1	0.2	11.9	0.0	0	124.4	
1958	126.8	166.8	93.0	53.0	0.0370%	11.6	0.0	11.6	0.0	0	115.2	
1957	117.3	159.3	90.2	48.2	0.0357%	9.7	0.1	9.6	0.0	0	107.6	
1956	111.9	155.5	87.3	43.7	0.0370%	9.4	0.3	9.1	0.0	0	102.5	
1955	105.8	151.5	85.4	39.7	0.0370%	9.0	0.3	8.7	0.0	0	96.8	
1954	99.7	144.2	81.8	37.3	0.0357%	7.8	0.1	7.7	0.0	0	91.9	
1953	94.2	138.7	78.5	34.0	0.0357%	7.3	0.1	7.2	0.0	0	86.9	
1952	88.6	131.0	73.7	31.3	0.0370%	7.8	0.8	7.0	0.0	0	80.8	
1951	83.5	124.3	70.0	29.2	0.0370%	6.6	0.0	6.6	0.0	0	76.9	
1950	84.8	122.9	68.7	30.6	0.0370%	7.8	1.4	6.4	0.0	0	77.0	
1949	151.1	122.7	0.0	28.4	0.0833%	6.4	0.3	6.1	0.0	0	144.7	
1948	145.6	119.3	0.0	26.3	0.0833%	7.0	0.7	6.3 <sup>6</sup>	0.0	0	138.6	
1947	157.5	114.4	0.0	43.1	0.0833%	9.9	0.1	9.8	0.0	0	147.6	
1946	130.7	107.0	0.0	23.7	0.0833%	10.0	0.1	9.9	0.0	0	120.7	
1945	121.0	93.7	0.0	27.3	0.0833%	9.4	0.1	9.3	0.0	0	111.6	
1944	99.3	80.9	0.0	18.4	0.0833%	9.3	0.1	9.2	0.0	0	90.0	
1943	86.6	70.0	0.0	16.6	0.0833%	9.8	0.2	9.6	0.0	0	76.8	
1942	69.1	56.5	0.0	12.6	0.0833%	10.1	0.5	9.6	0.0	0	59.0	
1941	62.0	51.4	0.0	10.6	0.0833%	10.1	0.6	9.5	0.0	0	51.9	
1940	55.9	46.2	0.0	9.7	0.0833%	12.9	3.5	9.4	0.0	0	43.0	
1939	51.2	40.7	0.0	10.5	0.0833%	16.4	7.2	9.2	0.0	0	34.8	
1938	47.7	38.3	0.0	9.4	0.0833%	11.3	2.5	8.8	0.0	0	36.4	
1937	48.2	38.8	0.0	9.4	0.0833%	12.2	3.7	8.5	0.0	0	36.0	
1936	43.8	35.6	0.0	8.2	0.0833%	10.9	2.6	8.3	0.0	0	32.9	
1935	20.8	11.5	0.0	9.3	0.0833%	11.3	2.8	8.5	0.0	0	9.5	
1933/4	7.0	0.0	0.0	7.0	N/A	10.0	0.2	9.8	0.0	0	(3.0)	

<sup>1</sup> The effective rates from 1950 through 1984 vary from the statutory rate of 0.0833 percent due to assessment credits provided in those years. The statutory rate increased to 0.12 percent in 1990 and to a minimum of 0.15 percent in 1991. The effective rates in 1991 and 1992 vary because the FDIC exercised new authority to increase assessments above the statutory rate when needed. Beginning in 1993, the effective rate is based on a risk-related premium system under which institutions pay assessments in the range of 0.23 percent to 0.31 percent. In May 1995, the BIF reached the mandatory recapitalization level of 1.25 percent. As a result, the assessment rate was reduced to 4.4 cents per \$100 of insured deposits and assessment premiums totaling \$1.5 billion were refunded in September 1995.

<sup>2</sup> These expenses, which are presented as operating expenses in the Statements of Income and Fund Balance, pertain to the FDIC in its corporate capacity only and **do not** include costs that are charged to the failed bank receiverships that are managed by the FDIC. The receivership expenses are presented as part of the "Receivables from Resolutions, net" line on the Balance Sheets. The information presented in the "FDIC Expenditures" table on page 108 of this report shows the aggregate (corporate and receivership) expenditures of the FDIC.

<sup>3</sup> Includes \$210 million for the cumulative effect of an accounting change for certain postretirement benefits.

<sup>4</sup> Includes \$105.6 million net loss on government securities.

<sup>5</sup> This amount represents interest and other insurance expenses from 1933 to 1972.

<sup>6</sup> Includes the aggregate amount of \$80.6 million of interest paid on capital stock between 1933 and 1948.

**Recoveries and Losses by the Deposit Insurance Fund on Disbursements for the Protection of Depositors,  
1934 through 2006**

Dollars in Thousands

All Cases <sup>1</sup>							
Year	Number of Banks/ Thrifts	Total Assets	Total Deposits	Disbursements	Recoveries	Estimated Additional Recoveries	Estimated Losses
<b>Total</b>	<b>2,234</b>	<b>\$ 301,400,469</b>	<b>\$ 246,367,303</b>	<b>\$ 114,990,538</b>	<b>\$ 76,073,360</b>	<b>\$ 554,078</b>	<b>\$ 38,363,100</b>
2006	0	0	0	0	0	0	0
2005	0	0	0	0	0	0	0
2004	4	165,866	145,885	138,895	133,905	1,167	3,823
2003	3	1,096,724	903,504	883,772	681,532	132,255	69,985
2002	11	2,557,811	2,175,043	2,068,519	1,570,551	106,623	391,345
2001	4	2,234,253	1,610,474	1,605,147	1,057,206	268,182	279,759
2000	7	407,618	340,533	297,313	265,175	0	32,138
1999	8	1,486,775	1,331,578	1,307,045	662,773	28,614	615,658
1998	3	370,400	335,076	286,678	52,248	8,312	226,118
1997	1	25,921	26,800	25,546	20,520	0	5,026
1996	6	215,078	200,973	201,533	140,937	0	60,596
1995	6	753,024	632,700	609,043	524,571	0	84,472
1994	13	1,392,140	1,236,488	1,224,769	1,045,718	0	179,051
1993	42	4,405,373	3,827,177	3,841,658	3,198,503	902	642,253
1992	122	44,231,922	41,184,366	14,175,372	10,506,358	1,038	3,667,976
1991	127	63,203,713	53,832,141	21,196,493	15,197,510	2,586	5,996,397
1990	169	15,676,700	14,488,900	10,817,419	8,034,946	4,399	2,778,074
1989	207	29,168,596	24,090,551	11,445,829	5,248,247	0	6,197,582
1988	280	70,065,789	45,499,102	12,163,006	5,244,866	0	6,918,140
1987	203	9,366,300	8,399,500	5,037,871	3,015,215	0	2,022,656
1986	145	7,710,400	7,056,700	4,790,969	3,015,252	0	1,775,717
1985	120	8,741,268	8,059,441	2,920,687	1,913,452	0	1,007,235
1984	80	3,276,411	2,883,162	7,696,215	6,056,061	0	1,640,154
1983	48	7,026,923	5,441,608	3,807,082	2,400,044	0	1,407,038
1982	42	11,632,415	9,908,379	2,275,150	1,106,579	0	1,168,571
1981	10	4,863,898	3,829,936	888,999	107,221	0	781,778
1980	11	244,117	221,302	152,355	121,675	0	30,680
1934-79	562	11,081,034	8,705,984	5,133,173	4,752,295	0	380,878

Deposit Assumption Cases							
Year	Number of Banks/ Thrifts	Total Assets	Total Deposits	Disbursements	Recoveries	Estimated Additional Recoveries	Estimated Losses
<b>Total</b>	<b>1,484</b>	<b>\$ 222,595,870</b>	<b>\$ 185,201,955</b>	<b>\$ 87,424,798</b>	<b>\$ 58,624,845</b>	<b>\$ 450,795</b>	<b>\$ 28,349,158</b>
2006	0	0	0	0	0	0	0
2005	0	0	0	0	0	0	0
2004	3	150,520	132,880	132,781	127,791	1,167	3,823
2003	3	1,096,724	903,504	883,772	681,532	132,255	69,985
2002	6	569,332	511,782	483,461	338,759	7,739	136,963
2001	4	2,234,253	1,610,474	1,605,147	1,057,206	268,182	279,759
2000	7	407,618	340,533	297,313	265,175	0	32,138
1999	8	1,486,775	1,331,578	1,307,045	662,773	28,614	615,658
1998	3	370,400	335,076	286,678	52,248	8,312	226,118
1997	1	25,921	26,800	25,546	20,520	0	5,026
1996	6	215,078	200,973	201,533	140,937	0	60,596
1995	6	753,024	632,700	609,043	524,571	0	84,472
1994	13	1,392,140	1,236,488	1,224,769	1,045,718	0	179,051
1993	37	4,098,618	3,556,005	3,580,297	3,035,754	902	543,641
1992	95	42,147,689	39,132,496	12,280,562	9,103,936	1,038	3,175,588
1991	103	61,593,332	52,274,435	19,938,700	14,410,415	2,586	5,525,699
1990	148	13,138,300	12,215,600	8,629,084	6,390,785	0	2,238,299
1989	174	26,811,496	21,931,451	9,326,725	3,985,855	0	5,340,870
1988	164	34,421,089	23,652,902	9,180,495	4,232,545	0	4,947,950
1987	133	4,311,700	4,020,700	2,773,202	1,613,502	0	1,159,700
1986	98	5,657,100	5,217,200	3,476,140	2,209,924	0	1,266,216
1985	87	2,235,182	2,000,044	1,631,166	1,095,601	0	535,565
1984	62	1,905,924	1,603,923	1,373,198	941,674	0	431,524
1983	35	3,194,452	2,275,313	2,893,969	1,850,553	0	1,043,416
1982	25	681,025	552,436	268,372	213,578	0	54,794
1981	5	4,808,042	3,778,486	79,208	71,358	0	7,850
1980	7	218,332	199,846	138,623	110,248	0	28,375
1934-79	251	8,671,804	5,528,330	4,797,969	4,441,887	0	356,082

**Recoveries and Losses by the Deposit Insurance Fund on Disbursements for the Protection of Depositors, 1934 through 2006** (continued)

Dollars in Thousands

Deposit Payoff Cases <sup>2</sup>							
Year	Number of Banks/ Thrifts	Total Assets	Total Deposit	Disbursements	Recoveries	Estimated Additional Recoveries	Estimated Losses
<b>Total</b>	<b>609</b>	<b>\$ 18,687,250</b>	<b>\$ 17,157,091</b>	<b>\$ 15,935,384</b>	<b>\$ 11,248,640</b>	<b>\$ 103,283</b>	<b>\$ 4,583,461</b>
2006	0	0	0	0	0	0	0
2005	0	0	0	0	0	0	0
2004	1	15,346	13,005	6,114	6,114	0	0
2003	0	0	0	0	0	0	0
2002	5	1,988,479	1,663,261	1,585,058	1,231,792	98,884	254,382
2001	0	0	0	0	0	0	0
2000	0	0	0	0	0	0	0
1999	0	0	0	0	0	0	0
1998	0	0	0	0	0	0	0
1997	0	0	0	0	0	0	0
1996	0	0	0	0	0	0	0
1995	0	0	0	0	0	0	0
1994	0	0	0	0	0	0	0
1993	5	306,755	271,172	261,361	162,749	0	98,612
1992	25	2,049,320	2,018,402	1,893,324	1,401,186	0	492,138
1991	21	1,526,538	1,477,328	1,251,676	784,002	0	467,674
1990	20	2,522,500	2,257,700	2,183,400	1,641,564	4,399	537,437
1989	32	2,280,100	2,086,100	2,116,556	1,262,140	0	854,416
1988	36	1,276,700	1,278,400	1,252,160	822,612	0	429,548
1987	51	2,539,000	2,260,800	2,103,792	1,401,000	0	702,792
1986	40	1,334,500	1,253,900	1,155,981	739,659	0	416,322
1985	29	610,156	548,986	523,789	411,175	0	112,614
1984	16	855,568	784,597	791,838	699,483	0	92,355
1983	9	164,037	160,998	148,423	122,484	0	25,939
1982	7	585,418	538,917	277,240	206,247	0	70,993
1981	2	51,018	47,536	35,736	34,598	0	1,138
1980	3	17,832	16,454	13,732	11,427	0	2,305
1934-79	307	563,983	479,535	335,204	310,408	0	24,796

Assistance Transactions							
Year	Number of Banks/ Thrifts	Total Assets	Total Deposits	Disbursements	Recoveries	Estimated Additional Recoveries	Estimated Losses
<b>Total</b>	<b>141</b>	<b>\$ 60,117,349</b>	<b>\$ 44,008,257</b>	<b>\$ 11,630,356</b>	<b>\$ 6,199,875</b>	<b>\$ 0</b>	<b>\$ 5,430,481</b>
2006	0	0	0	0	0	0	0
2005	0	0	0	0	0	0	0
2004	0	0	0	0	0	0	0
2003	0	0	0	0	0	0	0
2002	0	0	0	0	0	0	0
2001	0	0	0	0	0	0	0
2000	0	0	0	0	0	0	0
1999	0	0	0	0	0	0	0
1998	0	0	0	0	0	0	0
1997	0	0	0	0	0	0	0
1996	0	0	0	0	0	0	0
1995	0	0	0	0	0	0	0
1994	0	0	0	0	0	0	0
1993	0	0	0	0	0	0	0
1992	2	34,913	33,468	1,486	1,236	0	250
1991	3	83,843	80,378	6,117	3,093	0	3,024
1990	1	15,900	15,600	4,935	2,597	0	2,338
1989	1	77,000	73,000	2,548	252	0	2,296
1988	80	34,368,000	20,567,800	1,730,351	189,709	0	1,540,642
1987	19	2,515,600	2,118,000	160,877	713	0	160,164
1986	7	718,800	585,600	158,848	65,669	0	93,179
1985	4	5,895,930	5,510,411	765,732	406,676	0	359,056
1984	2	514,919	494,642	5,531,179	4,414,904	0	1,116,275
1983	4	3,668,434	3,005,297	764,690	427,007	0	337,683
1982	10	10,365,972	8,817,026	1,729,538	686,754	0	1,042,784
1981	3	4,838	3,914	774,055	1,265	0	772,790
1980	1	7,953	5,002	0	0	0	0
1934-79	4	1,845,247	2,698,119	0	0	0	0

<sup>1</sup> Totals do not include dollar amounts for the five open bank assistance transactions between 1971 and 1980. Excludes eight transactions prior to 1962 that required no disbursements. Also, disbursements, recoveries, and estimated additional recoveries do not include working capital advances to and repayments by receiverships.

<sup>2</sup> Includes insured deposit transfer cases.

Note:  
Beginning with the 1997 Annual Report, the number of banks in the Assistance Transactions column for 1988 was changed from 21 to 80 and the number of banks in the All Cases column was changed from 221 to 280 to reflect that one assistance transaction encompassed 60 institutions. Also, certain 1982, 1983, 1989 and 1992 resolutions previously reported in either the Deposit Payoff or Deposit Assumption categories were reclassified.

**Number, Assets, Deposits, Losses, and Loss to Funds of Insured Thrifts  
Taken Over or Closed Because of Financial Difficulties, 1989 through 1995<sup>1</sup>**

Dollars in Thousands

Year <sup>2</sup>	Total	Assets	Deposits	Estimated Receivership Loss <sup>3</sup>	Loss to Funds <sup>4</sup>
<b>Total</b>	<b>748</b>	<b>\$ 395,017,406</b>	<b>\$ 318,328,770</b>	<b>\$ 75,060,219</b>	<b>\$ 81,621,459</b>
1995	2	423,819	414,692	28,192	27,750
1994	2	136,815	127,508	11,472	14,599
1993	10	7,178,794	5,708,253	267,595	65,212
1992	59	44,196,946	34,773,224	3,220,731	3,765,968
1991	144	78,898,904	65,173,122	8,426,188	8,957,761
1990	213	129,662,498	98,963,962	16,017,169	19,212,063
1989 <sup>5</sup>	318	134,519,630	113,168,009	47,088,872	49,578,106

<sup>1</sup> Prior to July 1, 1995, all thrift closings were the responsibility of the Resolution Trust Corporation (RTC). Since the RTC was terminated on December 31, 1995, and all assets and liabilities transferred to the FSLIC Resolution Fund (FRF), all the results of the thrift closing activity from 1989 through 1995 are now reflected on FRF's books.

<sup>2</sup> Year is the year of failure, not the year of resolution.

<sup>3</sup> The estimated losses represent the projected loss at the fund level from receiverships for unreimbursed subrogated claims of the FRF and unpaid advances to receiverships from the FRF.

<sup>4</sup> The Loss to Funds represents the total resolution cost of the failed thrifts in the FRF-RTC funds, which includes corporate revenue and expense items such as interest expense on Federal Financing Bank debt, interest expense on escrowed funds, and interest revenue on advances to receiverships, in addition to the estimated losses for receiverships.

<sup>5</sup> Total for 1989 excludes nine failures of the former FSLIC.

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### FDIC Actions on Financial Institutions Applications 2004-2006

	2006	2005	2004
<b>Deposit Insurance</b>	<b>142</b>	219	176
Approved	142	219	176
Denied	0	0	0
<b>New Branches</b>	<b>1,257</b>	1,575	1,447
Approved	1,257	1,575	1,447
Denied	0	0	0
<b>Mergers</b>	<b>229</b>	286	311
Approved	229	286	311
Denied	0	0	0
<b>Requests for Consent to Serve*</b>	<b>138</b>	170	301
Approved	138	170	301
Section 19	11	13	13
Section 32	127	157	288
Denied	0	0	0
Section 19	0	0	0
Section 32	0	0	0
<b>Notices of Change in Control</b>	<b>3</b>	9	18
Letters of Intent Not to Disapprove	2	9	18
Disapproved	1	0	0
<b>Brokered Deposit Waivers</b>	<b>26</b>	40	32
Approved	26	40	32
Denied	0	0	0
<b>Savings Association Activities*</b>	<b>33</b>	59	70
Approved	33	59	70
Denied	0	0	0
<b>State Bank Activities/Investments†</b>	<b>14</b>	18	27
Approved	14	18	27
Denied	0	0	0
<b>Conversions of Mutual Institutions</b>	<b>9</b>	11	12
Non-Objection	9	11	12
Objection	0	0	0

\* Under Section 19 of the Federal Deposit Insurance (FDI) Act, an insured institution must receive FDIC approval before employing a person convicted of dishonesty or breach of trust. Under Section 32, the FDIC must also approve any change of directors or senior executive officers at a state nonmember bank that is not in compliance with capital requirements or is otherwise in troubled condition.

† Amendments to Part 303 of the FDIC Rules and Regulations changed FDIC oversight responsibility in October 1998. In 1998, Part 303 changed the Delegations of Authority to act upon applications.

‡ Section 24 of the FDI Act, in general, precludes a federally insured state bank from engaging in an activity not permissible for a national bank and requires notices to be filed with the FDIC.

### Compliance, Enforcement and Other Related Legal Actions 2004-2006

	2006	2005	2004
<b>Total Number of Actions Initiated by the FDIC</b>	<b>244</b>	192	217
<b>Termination of Insurance</b>			
<b>Involuntary Termination</b>			
Sec. 8a For Violations, Unsafe/Unsound Practices or Condition	0	0	0
<b>Voluntary Termination</b>			
Sec. 8a By Order Upon Request	1	0	0
Sec. 8p No Deposits	2	2	2
Sec. 8q Deposits Assumed	3	11	38
<b>Sec. 8b Cease-and-Desist Actions</b>			
Notices of Charges Issued	0	0	0
Consent Orders	29	20	28
<b>Sec. 8e Removal/Prohibition of Director or Officer</b>			
Notices of Intention to Remove/Prohibit	3	2	3
Consent Orders	89	73	58
<b>Sec. 8g Suspension/Removal When Charged With Crime</b>	<b>0</b>	0	1
<b>Civil Money Penalties Issued</b>			
Sec. 7a Call Report Penalties	0	0	0
Sec. 8i Civil Money Penalties	93	69	68
<b>Sec. 10c Orders of Investigation</b>	<b>17</b>	15	15
<b>Sec. 19 Denials of Service After Criminal Conviction</b>	<b>0</b>	0	1
<b>Sec. 32 Notices Disapproving Officer/Director's Request for Review</b>	<b>0</b>	0	0
<b>Truth-in-Lending Act Reimbursement Actions</b>			
Denials of Requests for Relief	0	0	0
Grants of Relief	2	0	0
Banks Making Reimbursement*	110	78	73
<b>Suspicious Activity Reports (Open and closed institutions)*</b>	<b>119,384</b>	102,080	83,453
<b>Other Actions Not Listed*</b>	<b>5</b>	0	3

\*These actions do not constitute the initiation of a formal enforcement action and, therefore, are not included in the total number of actions initiated.

\*Other Actions Not Listed includes Written Agreements, Section 19 Waiver grants, Section 8(e) Modifications, and similar actions in which orders are issued.

## Appendix B – More About the FDIC

### FDIC Board of Directors

Martin J. Gruenberg, Sheila C. Bair, Chairman (seated),  
John C. Dugan, Thomas J. Curry, and John M. Reich (standing, left to right)



### Sheila C. Bair

Sheila C. Bair was sworn in as the 19th Chairman of the Federal Deposit Insurance Corporation (FDIC) on June 26, 2006. She was appointed Chairman for a five-year term, and as a member of the FDIC Board of Directors through July 2013.

Before her appointment to the FDIC, Ms. Bair was the Dean's Professor of Financial Regulatory Policy for the Isenberg School of Management at the University of Massachusetts-Amherst since 2002. Other career

experience includes serving as Assistant Secretary for Financial Institutions at the U.S. Department of the Treasury (2001 to 2002), Senior Vice President for Government Relations of the New York Stock Exchange (1995 to 2000), a Commissioner and Acting Chairman of the Commodity Futures Trading Commission (1991 to 1995), and Research Director, Deputy Counsel and Counsel to Senate Majority Leader Robert Dole (1981 to 1988).

While an academic, Chairman Bair also served on the FDIC's Advisory Committee on Banking Policy.

Chairman Bair's prior work focused heavily on the banking sector. As the Assistant Treasury Secretary for Financial Institutions, she was charged with helping to develop the Administration's positions on banking policy issues. She worked closely with Treasury's own banking regulatory bureaus, the Office of



the Comptroller of the Currency and the Office of Thrift Supervision, as well as the Federal Reserve Board and the FDIC. Ms. Bair's teaching and research at the University of Massachusetts also dealt extensively with banking and related issues.

Ms. Bair has served as a member of several professional and non-profit organizations, including the Insurance Marketplace Standards Association, Women in Housing and Finance, Center for Responsible Lending, NASD Ahead-of-the-Curve Advisory Committee, Massachusetts Savings Makes Cents, American Bar Association, Exchequer Club, and Society of Children's Book Writers and Illustrators.

Five months after becoming Chairman, Ms. Bair was named to The Wall Street Journal magazine *Smart Money's* (November 2006) "Power 30" list – the magazine's lineup of the 30 most influential people in investing. Chairman Bair has also received several honors for her published work on financial issues, including her educational writings on money and finance for children, and for professional achievement. Among the honors she has received are: Distinguished Achievement Award, Association of Education Publishers (2005); Personal Service Feature of the Year, and Author of the Month Awards, *Highlights Magazine for Children* (2002, 2003 and 2004); and The Treasury Medal (2002). Her first book – *Rock, Brock and the Savings Shock*, a publication for children – was published in 2006.

Chairman Bair received a bachelor's degree from Kansas University and a J.D. from Kansas University School of Law. She is married to Scott P. Cooper and has two children.

## Martin J. Gruenberg

Martin J. Gruenberg was sworn in as Vice Chairman of the FDIC Board of Directors on August 22, 2005. Upon the resignation of Chairman Donald Powell, he served as Acting Chairman from November 15, 2005, to June 26, 2006.

Mr. Gruenberg joined the Board after broad congressional experience in the financial services and regulatory areas. He served as Senior Counsel to Senator Paul S. Sarbanes (D-MD) on the staff of the Senate Committee on Banking, Housing, and Urban Affairs from 1993 to 2005. Mr. Gruenberg advised the Senator on all issues of domestic and international financial regulation, monetary policy and trade. He also served as Staff Director of the Banking Committee's Subcommittee on International Finance and Monetary Policy from 1987 to 1992. Major legislation in which Mr. Gruenberg played an active role during his service on the Committee includes the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), the Gramm-Leach-Bliley Act, and the Sarbanes-Oxley Act of 2002.

Mr. Gruenberg holds a J.D. from Case Western Reserve Law School and an A.B. from Princeton University, Woodrow Wilson School of Public and International Affairs.

## Thomas J. Curry

Thomas J. Curry took office on January 12, 2004, as a member of the Board of Directors of the Federal Deposit Insurance Corporation for a six-year term. Mr. Curry serves as Chairman of the FDIC's Assessment Appeals Committee.

Mr. Curry also serves as the Chairman of the NeighborWorks® America Board of Directors. NeighborWorks® America is a national nonprofit organization chartered by Congress to provide financial support, technical assistance, and training for community-based neighborhood revitalization efforts.

Prior to joining the FDIC's Board of Directors, Mr. Curry served five Massachusetts Governors as the Commonwealth's Commissioner of Banks from 1990 to 1991 and from 1995 to 2003. He served as Acting Commissioner from February 1994 to June 1995. He previously served as First Deputy Commissioner and Assistant General Counsel within the Massachusetts Division of Banks. He entered state government in 1982 as an attorney with the Massachusetts Secretary of State's Office.

Director Curry served as the Chairman of the Conference of State Bank Supervisors from 2000 to 2001. He served two terms on the State Liaison Committee of the Federal Financial Institutions Examination Council, including a term as Committee chairman.

He is a graduate of Manhattan College (summa cum laude), where he was elected to Phi Beta Kappa. He received his law degree from the New England School of Law.

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## **John C. Dugan**

John C. Dugan was sworn in as the 29th Comptroller of the Currency on August 4, 2005. In addition to serving as a director of the FDIC, Comptroller Dugan also serves as a director of the Federal Financial Institutions Examination Council and NeighborWorks® America.

Prior to his appointment as Comptroller, Mr. Dugan was a partner at the law firm of Covington & Burling, where he chaired the firm's Financial Institutions Group. He specialized in banking and financial institution regulation. He also served as outside counsel to the ABA Securities Association.

He served at the Department of Treasury from 1989 to 1993 and was appointed assistant secretary for domestic finance in 1992. In 1991, he oversaw a comprehensive study of the banking industry that formed the basis for the financial modernization legislation proposed by the administration of the first President Bush. From 1985 to 1989, Mr. Dugan was minority counsel and minority general counsel for the U.S. Senate Committee on Banking, Housing, and Urban Affairs.

Among his professional and volunteer activities before becoming Comptroller, he served as a director of Minbanc, a charitable organization whose mission is to enhance professional and educational opportunities for minorities in the banking industry. He was also a member of the American Bar Association's committee on banking law, the Federal Bar Association's section of financial institutions and the economy, and the District of Columbia Bar Association's section of corporations, finance, and securities laws.

A graduate of the University of Michigan in 1977 with an A.B. in English literature, Mr. Dugan also earned his J.D. from Harvard Law School in 1981.

## **John M. Reich**

John M. Reich was sworn in August 9, 2005, as Director of the Office of Thrift Supervision (OTS). The President nominated Mr. Reich to be OTS Director on June 7, 2005, and the Senate confirmed his nomination on July 29, 2005. In this capacity, Mr. Reich will continue to serve as a member of the Board of Directors of the FDIC.

Prior to joining OTS, Mr. Reich served as Vice Chairman of the Board of Directors of the Federal Deposit Insurance Corporation (FDIC) since November 2002. He has been a member of the FDIC Board since January 2001. He also served as Acting Chairman of the FDIC from July to August 2001.

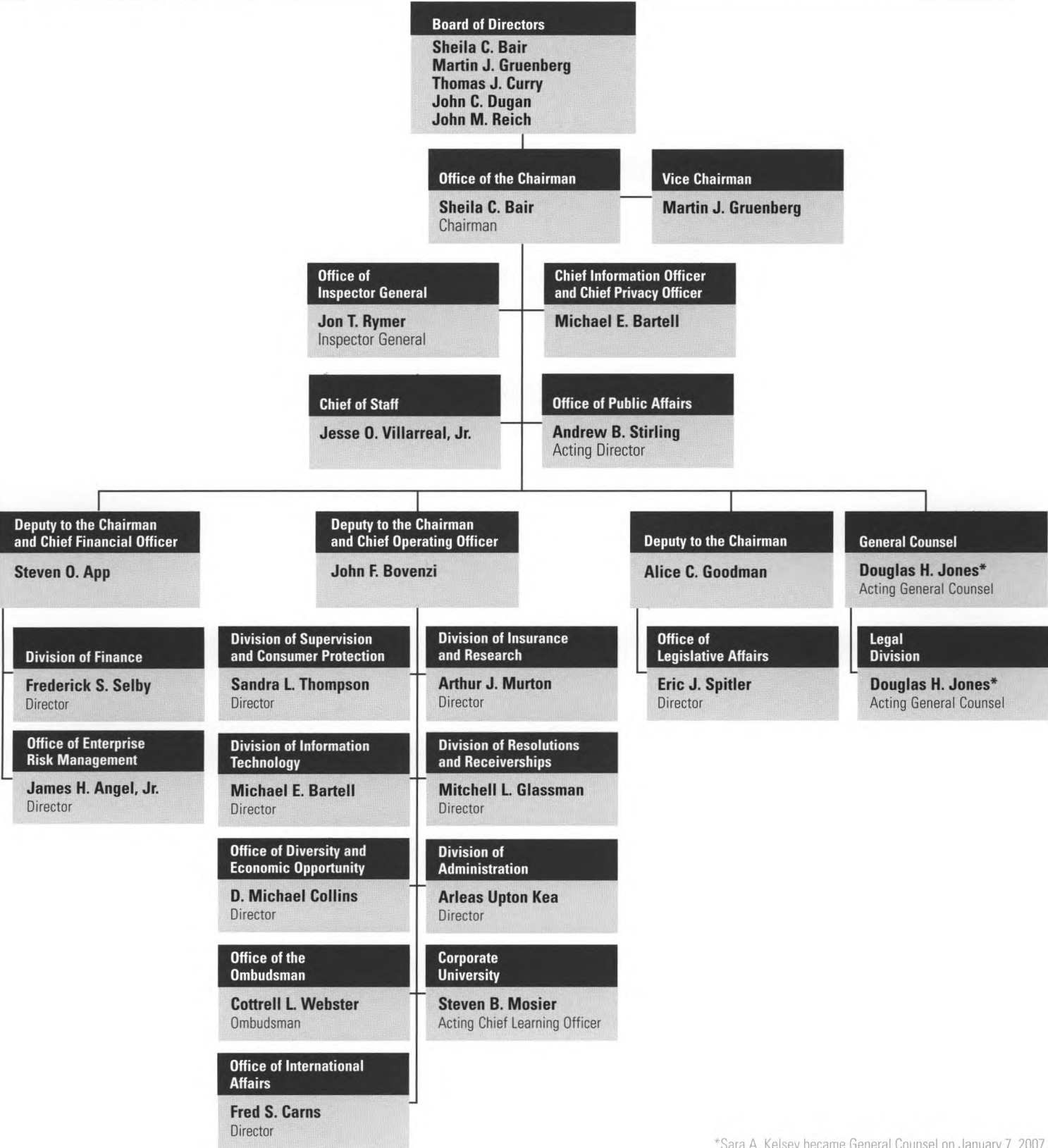
Prior to coming to Washington, DC, Mr. Reich spent 23 years as a community banker in Illinois and Florida, including ten years as President and CEO of the National Bank of Sarasota, in Sarasota, Florida.

Mr. Reich also served 12 years on the staff of U.S. Senator Connie Mack (R-FL), before joining the FDIC. From 1998 through 2000, he was Senator Mack's Chief of Staff, directing and overseeing all of the Senator's offices and committee activities, including those at the Senate Banking Committee.

Mr. Reich's community service includes serving as Chairman of the Board of Trustees of a public hospital facility in Ft. Myers, FL, and Chairman of the Board of Directors of the Sarasota Family YMCA. He has also served as a Board member for a number of civic organizations, and was active for many years in youth baseball programs.

Mr. Reich holds a B.S. degree from Southern Illinois University and an M.B.A. from the University of South Florida. He is also a graduate of Louisiana State University's School of Banking of the South.

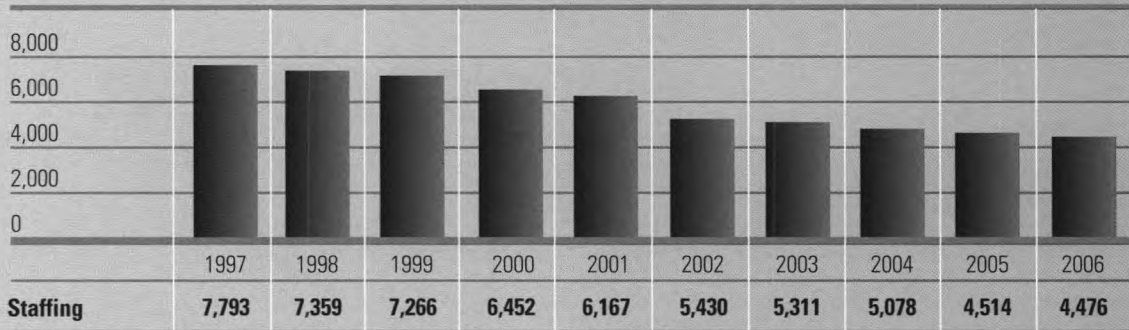
**FDIC Organization Chart/Officials**  
as of December 31, 2006



\*Sara A. Kelsey became General Counsel on January 7, 2007.

## Corporate Staffing

**Staffing Trends 1997-2006**



Note:  
All staffing totals reflect year-end balances.

**Number of Officials and Employees of the FDIC 2005-2006 (year-end)**

	Total		Washington		Regional/Field	
	2006	2005	2006	2005	2006	2005
Executive Offices*	39	37	39	37	0	0
Division of Supervision and Consumer Protection	2,517	2,541	195	198	2,322	2,343
Division of Resolutions and Receiverships	231	235	57	61	174	174
Legal Division	413	433	263	274	150	159
Division of Finance	161	175	161	175	0	0
Division of Information Technology†	274	270	214	209	60	61
Division of Insurance and Research	185	178	152	146	33	32
Division of Administration	311	349	207	232	104	117
Office of Inspector General	124	127	91	95	33	32
Office of Diversity and Economic Opportunity	28	31	28	31	0	0
Office of the Ombudsman	12	12	10	10	2	2
Office of Enterprise Risk Management	11	11	11	11	0	0
Corporate University	170	115	38	37	132	78
<b>Total</b>	<b>4,476</b>	<b>4,514</b>	<b>1,466</b>	<b>1,516</b>	<b>3,010</b>	<b>2,998</b>

\* Includes the Offices of the Chairman, Vice Chairman, Director (Appointive), Chief Operating Officer, Chief Financial Officer, Chief Information Officer, Legislative Affairs, Public Affairs and International Affairs.

† Division of Information Resources Management was renamed to Division of Information Technology on September 4, 2005.

## Sources of Information

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### Home Page on the Internet

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**www.fdic.gov**

A wide range of banking, consumer and financial information is available on the FDIC's Internet home page. This includes the FDIC's Electronic Deposit Insurance Estimator (EDIE), which estimates an individual's deposit insurance coverage; the Institution Directory—financial profiles of FDIC-insured institutions; Community Reinvestment Act evaluations and ratings for institutions supervised by the FDIC; Call Reports—banks' reports of condition and income; and *Money Smart*, a training program to help individuals outside the financial mainstream enhance their money management skills and create positive banking relationships. Readers also can access a variety of consumer pamphlets, FDIC press releases, speeches and other updates on the agency's activities, as well as corporate databases and customized reports of FDIC and banking industry information.

### FDIC Call Center

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**Phone: 877-275-3342  
(877-ASK FDIC)  
703-562-2222**

**Hearing  
Impaired: 800-925-4618**

The FDIC Call Center in Washington, DC, is the primary telephone point of contact for general questions from the banking community, the public and FDIC employees. The Call Center directly, or in concert with other FDIC subject-matter experts, responds to questions about deposit insurance and other consumer issues and concerns, as well as questions about FDIC programs and activities. The Call Center also makes referrals to other federal and state agencies as needed. Hours of operation are 8:00 a.m. to 8:00 p.m. Eastern Time. Information is also available in Spanish. Recorded information about deposit insurance and other topics is available 24 hours a day at the same telephone number.

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**Public Information Center  
3501 Fairfax Drive  
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(877-ASK FDIC), or  
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FDIC publications, press releases, speeches and Congressional testimony, directives to financial institutions, policy manuals and other documents are available on request or by subscription through the Public Information Center. These documents include the *Quarterly Banking Profile*, *FDIC Consumer News* and a variety of deposit insurance and consumer pamphlets.

### Office of the Ombudsman

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The Office of the Ombudsman (OO) is an independent, neutral and confidential resource and liaison for the banking industry and the general public. The OO responds to inquiries about the FDIC in a fair, impartial and timely manner. It researches questions and complaints primarily from bankers. The OO also recommends ways to improve FDIC operations, regulations and customer service.

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South Carolina

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Indiana  
Kentucky  
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Ohio

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### Dallas Regional Office

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Idaho

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Wyoming

## Appendix C – Office of Inspector General’s Assessment of the Management and Performance Challenges Facing the FDIC

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In keeping with the Reports Consolidation Act, the OIG has identified the following management and performance challenges facing the Corporation.<sup>•</sup> Each of the challenges we have identified is marked by one or more of the following characteristics:

1. It is important to the achievement of the FDIC mission and the strength of the nation’s financial system.
2. It directly impacts consumers of financial services.
3. It involves significant resources, expenditures, or fiduciary responsibility.

The following challenges reflect the OIG’s view of the Corporation’s overall program and operational responsibilities; industry, economic, and technological trends; areas of congressional interest; relevant laws and regulations; the Corporation’s priorities and corresponding corporate performance and Government Performance and Results Act goals; and the ongoing activities to address the issues involved.

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### Identifying and Mitigating Risks to the Insurance Funds

As of the end of the third quarter of 2006, the FDIC insured \$4.095 trillion in deposits in 8,755 institutions. According to FDIC projections, if the current trend of industry consolidation continues, the banks the FDIC directly supervises will likely represent a smaller and smaller portion of the financial exposure it faces as deposit insurer. In fact, as of June 30, 2006, the ten largest FDIC-insured institutions controlled 44 percent of total insured assets and 42 percent of total insured deposits. The FDIC is the primary federal regulator for none of these institutions. The Corporation is also working to maintain strong regulatory capital standards under the Basel Accord and has been implementing major reforms in deposit insurance over the past ten months. Given these circumstances, the Corporation faces several challenges:

#### **Assessing Risks in Large Banks:**

To effectively fulfill its fundamental responsibilities as deposit insurer, the Corporation must ensure its large-bank program provides ready access to the information it needs to effectively identify and assess risks that large institutions, including those it does not supervise, pose to the Deposit Insurance Fund (DIF). Effectively communicating and coordinating with the other primary federal banking regulators is central to the Corporation’s ability to meet this challenge. Moreover, given the inherent complexity of these large institutions, the FDIC must have or develop the capability to assess the risks associated with these institutions, which are different from those found in smaller banks. To strengthen its oversight of large banks, the Corporation has implemented some key programs: the Large Insured Depository Institutions program, Dedicated Examiner program, and Off-site Review program. The FDIC participates with the other federal regulators in the Shared National Credit program.

<sup>•</sup> Under the Reports Consolidation Act, the OIG is required to identify the most significant management and performance challenges facing the Corporation and provide its assessment to the Corporation for inclusion in its annual performance and accountability report (annual report). The OIG conducts this assessment yearly and identifies a number of specific areas of challenge facing the Corporation at the time.



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***Maintaining Strong Regulatory Capital Standards:***

The FDIC and other regulators have evaluated policy options to ensure that large institutions and the industry as a whole maintain adequate capital and reserves under Basel II. The intent of Basel II is to more closely align regulatory capital with risk in large or multinational banks. In conjunction with the transition to Basel II, the FDIC and the other federal bank regulatory agencies are pursuing a more risk-sensitive capital framework for the institutions that are not subject to or that opt out of Basel II. This new Basel IA capital framework seeks to minimize potential inequities between large and small banks resulting from Basel II implementation while maintaining adequate capital levels and avoiding undue burden on the affected institutions.

In 2007, the federal bank regulatory agencies will review comments received in response to Basel II and Basel IA notices of proposed rulemaking, complete rulemaking for Basel IA, and eventually seek to make final rules for Basel II.

***Implementing Deposit Insurance Reform:***

On February 8, 2006, President Bush signed into law the FDI Reform Act of 2005, prompting sweeping changes in the federal deposit insurance system. The Congress gave the Corporation nine months to implement most of the provisions of the legislation, and the Corporation has worked diligently to do so. In October 2006, the Board of Directors approved a final rule to implement a one-time assessment credit to banks and thrifts. The credit will be used to offset future assessments charged by the FDIC and will recognize contributions that certain institutions made to capitalize the funds during the first half of the 1990s. In November 2006, the Board also adopted a final rule on the pricing structure and approved a more risk-sensitive framework for the 95 percent of insured institutions that are well capitalized and well managed.

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**Ensuring Institution Safety and Soundness Through Effective Examinations, Enforcement, and Follow-Up**

Supervision is a cornerstone of the FDIC's efforts to ensure stability and public confidence in the nation's financial system. As of September 30, 2006, the FDIC was the primary federal regulator for 5,237 institutions. The FDIC performs risk management, information technology, trust, and other types of examinations of FDIC-supervised insured depository institutions. As part of risk management examinations, the FDIC also ensures that institutions comply with the regulatory requirements of the Bank Secrecy Act. The Corporation's system of supervisory controls must identify and effectively address financial institution activities that are unsafe, unsound, illegal, or improper before the activities cause a drain on the insurance funds. Specific challenges related to this core FDIC mission include:

***Maintaining an Effective Examination and Supervision Program:***

The FDIC has adopted a risk-focused approach to examinations to minimize regulatory burden and direct its resources to those areas that carry the greatest potential risk. The FDIC must also ensure that financial institutions have adequate corporate governance structures relative to the bank's size, complexity, and risk profile to prevent financial losses and maintain confidence in those entrusted with operating the institutions. The FDIC's follow-up processes must be effective to ensure institutions are promptly complying with supervisory actions that arise as a result of the FDIC's examination process.

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***Granting Insurance to and Supervising Industrial Loan Companies:***

The FDIC is the primary federal regulator for a number of industrial loan companies (ILCs), which are limited-charter depository institutions. ILCs may be owned by commercial firms, and these parents may not be subject to consolidated supervision by a federal banking regulator. As of September 30, 2006, there were 58 operating ILCs with aggregate total assets of \$177 billion. The FDIC must establish and maintain effective controls in its processes for granting insurance to, supervising, and examining ILCs, taking into consideration the relationship between the ILC and its parent company and the effect of such a relationship on the ILC. This is particularly important when the ILC's holding company is not subject to the scope of consolidated supervision, consolidated capital requirements, or enforcement actions imposed on parent organizations subject to the Bank Company Holding Act.

In July 2006, the FDIC placed a six-month moratorium on ILC deposit insurance applications and change of control notices. The Corporation wanted time to assess developments in the ILC industry; determine whether any emerging safety and soundness or policy issues exist; and evaluate whether statutory, regulatory, or policy changes needed to be made in the oversight of these institutions. While the moratorium is set to expire at the end of January, a number of congressional representatives have voiced concern over mixing banking and commerce and have urged the Corporation to extend its freeze on granting industrial loan charters to commercial applicants. This issue will continue to require FDIC attention.

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**Contributing to Public Confidence  
in Insured Depository Institutions**

***Guarding Against Financial Crimes in Insured Institutions:***

All financial institutions are at risk of being used to facilitate or being victimized by criminal activities including money laundering and terrorist financing. Such activities serve to undermine public confidence in the nation's financial system. The Corporation is faced with developing and implementing programs to minimize the extent to which the institutions it supervises are involved in or victims of financial crimes and other abuse. Increased reliance by both financial institutions and non-financial institution lenders on third-party brokers has also created opportunities for increased real-estate frauds, including property flipping and other mortgage frauds. Examiners must be alert to the possibility of multiple types of fraudulent activity in financial institutions, which is inherently difficult because fraud is both purposeful and hard to detect.

Part of the FDIC's overall responsibility and authority to examine banks for safety and soundness is the responsibility for examining state-chartered non-member financial institutions for compliance with the Bank Secrecy Act (BSA). The BSA requires financial institutions to keep records and file reports on certain financial transactions. FDIC-supervised institutions must establish and maintain procedures to assure and monitor compliance with BSA requirements. An institution's level of risk for potential money laundering determines the necessary scope of the BSA examination. In a related vein, the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC) promulgates, develops, and administers economic and trade sanctions such as trade embargoes, blocked assets controls, and other commercial and financial restrictions under the provisions of various laws. Generally, OFAC regulations prohibit financial institutions from engaging in transactions with the governments of, or individuals or entities associated with, foreign countries against which federal law imposes economic sanctions. Sanctions

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can also be used against international drug traffickers, terrorists, or foreign terrorist organizations, regardless of national affiliation. A challenge for the FDIC is to provide effective supervision of compliance with OFAC regulations by FDIC-supervised institutions.

In its role as supervisor, the FDIC also analyzes data security threats, occurrences of bank security breaches, and incidents of electronic crime that involve financial institutions. Misuse and misappropriation of personal information are emerging as major developments in financial crime. Despite generally strong controls and practices by financial institutions, methods for stealing personal data and committing fraud with that data are continuously evolving. The FDIC must continue its work in assuring the security of customer data against such criminal activity to help maintain the public's trust and confidence in the banking system.

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**Protecting and Educating Consumers and Ensuring Compliance Through Effective Examinations, Enforcement, and Follow-up**

The FDIC protects consumers through its oversight of a variety of statutory and regulatory requirements aimed at safeguarding consumer privacy and preventing unfair and unscrupulous banking practices. Through community outreach efforts and technical assistance, the FDIC encourages lenders to work with members of their local communities in meeting the communities' credit needs and to serve the unbanked and underbanked members of their communities. Specific challenges include:

***Safeguarding the Privacy of Consumer Information:***

The FDIC implements regulations and conducts regularly scheduled examinations to verify that institutions comply with laws designed to protect personal information, which serve to guard against the growing threat of identity theft. The FDIC evaluates the adequacy of financial institutions' programs for securing customer data and may pursue informal or formal supervisory action if it finds a deficiency. Banks are increasingly using third-party servicers to provide support for core information and transaction processing functions and these servicers may operate domestically or abroad. Notwithstanding such reliance, the obligations of a financial institution to protect the privacy and security of customer information under U.S. laws and regulations remain in full effect. Thus, an added challenge for the Corporation in examining and enforcing compliance with consumer privacy and protection laws exists because the FDIC expects institutions to effectively manage the risks and adequately oversee the third-party service providers.

***Promoting Fairness and Inclusion in the Delivery of Information, Products, and Services to Consumers and Communities:***

FDIC Chairman Bair has stressed the importance of economic inclusion and has expressed concern that market mechanisms are not working as well as they should for low-to-moderate income families who must often pay high amounts for basic financial services that others obtain at far less cost. Many people lack the financial skills needed to analyze and compare products and their prices. Oftentimes the problem is the lack of disclosures that describe a product and its true costs in fair and simple terms. Another factor could be linked to aspects of safety and soundness regulation that could unnecessarily deter banks from serving the needs of their communities or create conditions that favor high-cost products. To address these concerns, in addition to the FDIC's existing *Money Smart* program, the Corporation is undertaking two new initiatives—a military lending initiative

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and a newly created Advisory Committee on Economic Inclusion. As the Chairman has pointed out, continuing dialogue among consumer advocates, regulators, and the banking industry is key to the challenge of closing the gap between what the unbanked and underbanked pay for credit and what those in the mainstream pay. The challenge is to balance the need for regulation while avoiding inappropriate or undue interference in legitimate business activities.

***Ensuring Compliance with Laws and Regulations and Follow-up on Violations:***

The FDIC has supervisory responsibilities for ensuring that the financial institutions it supervises comply with fair lending, disclosure, and various other consumer protection laws and regulations. The compliance examination is the primary means by which the FDIC determines the extent to which a financial institution is complying with these requirements. Over 20 consumer protection laws and related regulations are addressed by compliance examinations, including the Home Mortgage Disclosure Act, Fair Housing Act, Truth in Lending Act, Equal Credit Opportunity Act, and Fair and Accurate Credit Transaction Act. The FDIC also conducts Community Reinvestment Act examinations. The FDIC conducts visitations and investigations to review the compliance posture of newly chartered institutions coming under FDIC supervision or to follow up on an institution's progress on corrective actions. Investigations are used to follow up on a particular consumer's inquiries or complaints. The compliance program, including examination and follow-up supervisory attention on violations and other program deficiencies, helps to ensure that consumers and businesses obtain the benefits and protections afforded them by law. In instances where repeat violations occur, the FDIC must remain vigilant in ensuring appropriate corrective actions are taken.

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**Being Ready for Potential Institution Failures**

The FDIC is responsible for the resolution of failed banks or savings associations. The Corporation is required by law to protect taxpayers by prudently managing the Deposit Insurance Fund and to protect insured depositors by using the assets of the fund to pay insured deposits at the time of institution failure. The trend toward fewer failures over the past few years changes the nature of the challenge for the FDIC. The Corporation is exploring new strategies for planning for failing and failed institutions, including large or multiple bank failures. Catastrophic events such as the multiple hurricanes that occurred during 2005 – which can threaten institution stability – also underscore the need for the Corporation's readiness to respond.

Given the industry's increase in merger and acquisition activity, banks are becoming more geographically diverse and complex, and institutions are much larger than they have been historically. As a result, the FDIC could potentially face the challenge of handling a failing institution with a significantly larger number of insured deposits than it has had to in the past. The FDIC Board is soliciting comments on proposed improvements to the process of determining the insurance status of depositors of larger institutions in the event of a failure to facilitate the related deposit insurance claims process. The FDIC has also been developing a new claims determination system. The Corporation's ability to rapidly determine the insured status of deposit accounts is essential to resolving bank failures in the most cost-effective and least disruptive manner.

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**Promoting Sound Governance  
and Managing and Protecting Human,  
Financial, Information Technology,  
Physical, and Procurement Resources**

The FDIC must practice sound governance and effectively manage and utilize a number of critical strategic resources in order to carry out its mission successfully, particularly its human, financial, information technology (IT), physical, and procurement resources. The FDIC Board of Directors plays a critical role in this regard, and FDIC management has emphasized its stewardship responsibilities in its strategic planning process. A number of key management activities pose challenges to corporate leadership and managers, as discussed below:

***Corporate Governance and Enterprise Risk Management:***

The FDIC is managed by a five-person Board of Directors, all of whom are appointed by the President and confirmed by the Senate, with no more than three being from the same political party. At least one Board member must have State bank supervisory experience. The Board includes the Directors of the Office of the Comptroller of the Currency and the Office of Thrift Supervision. Given the inevitability of relatively frequent changes in the Board make-up, it is essential that a strong and sustainable governance process is in place and that Board members have and share the information needed at all times to make sound policy and management decisions.

As an important part of its governance process, the FDIC has established a risk management and internal control program. In the spirit of OMB Circular A-123, the Corporation has committed to adopting an enterprise risk management approach to identifying and analyzing risks on an integrated, corporate-wide basis. Revised OMB Circular A-123, which became effective for fiscal year 2006, requires a strengthened process for conducting management's assessment of the effectiveness of internal control over financial reporting. The circular also emphasizes the need for agencies to integrate and coordinate internal control assessments with other internal control-related activities, and ensure that an appropriate balance exists between the strength of controls and the relative risk associated with particular programs and operations.

***Human Capital Management:***

In the past several years, the FDIC has undergone significant restructuring and downsizing in response to changes in the industry, technological advances, and business process improvements and, as with many government agencies, the FDIC anticipates a high level of retirement in the next five years. Amidst such change, the Corporation formulated a human capital strategy to guide the FDIC through the rest of this decade. The FDIC Corporate University was created to play a key role in training, developing, and maintaining a highly skilled, professional workforce to carry out the FDIC mission. One of the initiatives it sponsors is the Corporate Employee Program, designed to help create a more adaptable permanent workforce that reflects a more collaborative and corporate approach to meeting critical mission functions. Additionally, developing new leaders and engaging in succession planning pose a challenge. In this regard, the Corporation has developed an Executive Candidate Development Program that it plans to pilot to identify high-potential employees to develop for future executive management positions. The Corporation also piloted a Talent Review Program this year that focused on executive succession management needs and executive development needs. Finally, in an age of identity theft risks, another challenge in human capital management is to maintain effective controls to protect personal employee-related information that the Corporation possesses. The appointment of a chief privacy officer and implementation of a privacy program have been positive steps in addressing that challenge.

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***Financial Management:***

The FDIC's operating expenses are largely paid from the insurance fund, and consistent with sound corporate governance principles, the Corporation must continuously seek to be efficient and cost-conscious. Because about 65 percent of the FDIC's budget costs are personnel-related, a challenge to the Corporation is to ensure that budgeted resources are properly aligned with workload. The Board approved a \$1.1 billion Corporate Operating Budget for 2007, approximately 4.6 percent higher than for 2006. The approved budget provides funding for additional compliance examiners, increased employee training, enhanced IT security and privacy programs, and completion of systems changes required to support the implementation of deposit insurance reform.

With respect to capital investments, effective planning and management of IT and non-IT capital investments are mandated by Congress and by the Office of Management and Budget for most federal agencies. Although many of these laws and executive orders are not legally binding on the FDIC, the Corporation recognizes that they constitute sound business practices and has decided to voluntarily adopt them in whole, or in part. The underlying financial management challenge facing the FDIC is to carry out approved investment projects on time and within budget, while realizing anticipated benefits. The Corporation's 2007 spending on multi-year investment projects separately approved by the Board is expected to be approximately \$19 million to \$23 million.

The Corporation is continuing to implement its New Financial Environment, intended to meet current and future financial management and financial information needs; improve corporate financial business processes; and redirect resources from transaction processing to analysis, risk management, and decision support.

***Information Technology Management:***

The FDIC seeks to maximize its IT resources to improve the efficiency and effectiveness of its operational processes. The Corporation operates a nationwide computing network and maintains more than 250 application systems for staff to carry out their responsibilities. To address IT management challenges, the FDIC must focus on the capital planning and investment processes for IT and maximize the effectiveness of the Chief Information Officer Council and Program Management Office, both of which play a continuing role in reviewing the portfolio of approved IT projects and other initiatives. The Corporation has also employed a new system development life cycle methodology to enhance its ability to effectively and efficiently manage IT project resources. It must also continue to enhance its Enterprise Architecture program by identifying duplicative resources/investments and opportunities for internal and external collaboration to promote operational improvements and cost-effective solutions to business requirements.

The establishment of an integrated and streamlined e-government infrastructure is a key component of the Corporation's target EA. In this regard, the Corporation has initiated a number of major projects designed to improve internal operations, communications, and service to members of the public, business, and other government entities. The challenge is to ensure that such projects are consistent with e-government principles and implementing guidance from the Office of Management and Budget.

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***IT and Physical Security:***

To achieve its mission, the FDIC relies on automated information systems to collect, process, and store vast amounts of banking and other sensitive information. Much of this information is used by financial regulators, academia, and the public to monitor bank performance, develop regulatory policy, and to research and analyze important banking issues. Ensuring the integrity, availability, and appropriate confidentiality of this information in an environment of increasingly sophisticated security threats and global connectivity requires a strong records management program and a correspondingly effective enterprise-wide information security program.

As a result of focused attention over the last several years, the FDIC has made significant progress in improving its information security program and practices. However, continued management attention is needed in certain key security control areas such as enterprise architecture, configuration management, access controls, and audit and accountability controls.

In light of past terrorist-related disruptions and, more recently, adverse impacts of natural disasters, the importance of corporate disaster recovery and business continuity planning has been underscored and elevated to an enterprise-wide level. The FDIC must be sure that its emergency response plans provide for the safety and physical security of its personnel and ensure that its business continuity planning and disaster recovery capability keep critical business functions operational during any emergency. Threats to public health such as a pandemic influenza could also put the Corporation's internal emergency preparedness to the test. In its role as a regulator, the Corporation has also joined with the other financial regulatory agencies in issuing an interagency advisory to financial institutions and their technology service providers to raise awareness regarding the threat of a pandemic influenza outbreak and its potential impact on the delivery of critical financial services.

***Procurement Management:***

Over the past few years, the FDIC has increased its reliance on outsourcing for services such as IT infrastructure support, IT application system development, and facilities maintenance. As of March 2006, in fact, the value of the FDIC's active contracts totaled over \$1.6 billion. The Corporation has also downsized and reduced its contracting staff over the same time frame, which has posed challenges to contract administration activities. Given this environment, effective and efficient processes and related controls for identifying needed goods and services, acquiring them, and monitoring contractors after the contract award must be in place and operate well. Also, a number of new contracting vehicles and approaches have been implemented. For example, the Corporation combined approximately 40 IT-related contracts into one contract with multiple vendors for a total program value of \$555 million over ten years. Also, for the first time, the FDIC is using a large technical infrastructure contract through the General Services Administration (GSA) valued at over \$340 million. Along with the expected benefits of these contracts come challenges. The Corporation has not previously outsourced a procurement process to GSA, and both new contracts are performance-based, requiring different oversight mechanisms and strategies than the time and materials contracts that the Corporation has historically used.

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**Federal  
Deposit  
Insurance  
Corporation**

This **Annual Report** was produced by talented and dedicated staff. To these individuals, we would like to offer our sincere thanks and appreciation. Special recognition is given to the following individuals for their contributions:

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