

WASHINGTON MUTUAL, INC  
Form 10-K/A  
May 22, 2008

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-K/A  
Amendment No. 1**

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

Commission File Number 1-14667

**WASHINGTON MUTUAL, INC.**

(Exact name of registrant as specified in its charter)

**Washington**  
(State or other jurisdiction of  
incorporation or organization)

**91-1653725**  
(I.R.S. Employer  
Identification Number)

**1301 Second Avenue, Seattle, Washington**  
(Address of principal executive offices)

**98101**  
(Zip Code)

Registrant's telephone number, including area code: **(206) 461-2000**

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

<b>Title of each class</b>	<b>Name of each exchange on which registered</b>
Common Stock	New York Stock Exchange
Depository Shares each representing a 1/40,000 <sup>th</sup> interest in a share of Series K Perpetual Preferred Non-Cumulative Floating Rate Stock	New York Stock Exchange
7.75% Series R Non-Cumulative Perpetual Convertible Preferred Stock	New York Stock Exchange

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

<b>Title of each class</b>	<b>Name of each exchange on which registered</b>
Litigation Tracking Warrants	NASDAQ

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

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

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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

The aggregate market value of voting stock held by non-affiliates of the registrant as of June 30, 2007, based on the closing sale price as reported on the New York Stock Exchange:

**Common Stock \$36,953,361,076**

<sup>(1)</sup> Does not include any value attributable to 6,000,000 shares held in escrow.

The number of shares outstanding of the issuer's classes of common stock as of January 31, 2008:

**Common Stock 882,557,330**

<sup>(2)</sup> Includes 6,000,000 shares held in escrow.

### Documents Incorporated by Reference

Portions of the definitive proxy statement for the Annual Meeting of Shareholders to be held April 15, 2008, are incorporated by reference into Part III.

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**WASHINGTON MUTUAL, INC.  
2007 ANNUAL REPORT ON FORM 10-K/A  
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**Explanatory Note**

Washington Mutual, Inc. ("Washington Mutual" or the "Company") is filing this Amendment No. 1 to its Annual Report on Form 10-K for the year ended December 31, 2007 originally filed on February 29, 2008 ("Original Filing") to include additional disclosures to certain information presented in Parts II and III. Such additional disclosures have no effect on previously reported consolidated financial statements and notes to consolidated financial statements.

This Amendment No. 1 on Form 10-K/A amends the Original Filing as follows:

Part II, Item 7 (Management's Discussion and Analysis of Financial Condition and Results of Operations) to include in the Credit Risk Management section the five-year table of changes in the allowance for loan losses and the related disclosure of factors considered in determining the changes to the yearly allowance during the five-year period (pages 51 and 52). The Company had previously included and continues to include the five-year table of changes in the allowance for loan losses in Note 6 "Loans and Allowance for Loan Losses" to the Consolidated Financial Statements.

Part II, Item 7 (Management's Discussion and Analysis of Financial Condition and Results of Operations) to include in the Credit Risk Management section additional disclosure in connection with the allocated allowance for loan losses table regarding changes in the allocated allowance for the home loans portfolio and the subprime mortgage channel portfolio (pages 54 and 55).

Part III, Item 11 (Executive Compensation) to furnish the Item 11 disclosures contained in the Company's definitive proxy statement issued in conjunction with the Company's Annual Meeting of Shareholders held on April 15, 2008 (the "Annual Proxy Statement") (pages 81 to 137), which disclosures were incorporated in the Original Filing by reference to the Annual Proxy Statement, and to add the following disclosures concerning the design of the Company's 2008 bonus plan (beginning after the first sentence of paragraph 1 on page 92): "In selecting and defining the net operating profit performance measure for 2008, a period when the Company was expecting to experience significantly elevated loan loss provision and foreclosed asset expense from its single-family residential mortgage loan portfolio, the Committee was focused on sustaining and growing the Company's top-line revenues and controlling other expenses. Sustaining and growing top-line revenues and controlling other expenses were seen as important to achieving the following objectives: (a) enabling the Company to return to longer-range earnings expectations after these elevated credit costs subside, and (b) helping ensure that the fundamental drivers of the Company's long-term franchise value would not be materially diminished during the period of elevated credit costs in its mortgage loan portfolios. The Committee believed that these objectives would provide a foundation for restoring shareholder value."

Except for the foregoing additional Item 11 disclosures, revised page cross-references and including a list of peer companies on page 96 that was included as Appendix A to the Annual Proxy Statement, the Item 11 disclosures from the Annual Proxy Statement are repeated verbatim and, together with the foregoing additional Item 11 disclosures and list of peer companies, speak as of the date of the Annual Proxy Statement. Except for Item 7 of Part II and Item 11 of Part III, no other information in the Original Filing is being amended by this Amendment. This Amendment continues to speak as of the date of the Original Filing and the Company has not updated the disclosure in this Amendment to reflect any events which occurred at a date subsequent to the Original Filing.

**PART II**

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**Controls and Procedures**

**Disclosure Controls and Procedures**

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or furnishes under the Securities Exchange Act of 1934.

Management reviews and evaluates the design and effectiveness of the Company's disclosure controls and procedures on an ongoing basis, which may result in the discovery of deficiencies, and improves its controls and procedures over time, correcting any deficiencies, as needed, that may have been discovered.

**Changes in Internal Control Over Financial Reporting**

Management reviews and evaluates the design and effectiveness of the Company's internal control over financial reporting on an ongoing basis, which may result in the discovery of deficiencies, some of which may be significant. Management changes its internal control over financial reporting as needed to maintain its effectiveness, correcting any deficiencies, as needed, in order to ensure the continued effectiveness of the Company's internal control over financial reporting. There have not been any changes in the Company's internal control over financial reporting during the fourth quarter of 2007 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. For management's assessment of the Company's internal control over financial reporting, refer to Management's Report on Internal Control Over Financial Reporting on page 98.

**Overview**

Washington Mutual, through its subsidiaries, is one of the nation's leading consumer and small business banks. At December 31, 2007, Washington Mutual and its subsidiaries had assets of \$328 billion. The Company has a history dating back to 1889 and its subsidiary banks currently operate nearly 2,500 consumer and small business banking stores throughout the nation. When we refer to "the Company," "we," "our" and "us" in this Annual Report on Form 10-K, we mean Washington Mutual, Inc. and subsidiaries. When we refer to "the Parent," we mean Washington Mutual, Inc.

The Company's sources of revenue are net interest income and noninterest income. Net interest income is generated by interest received from loans, investment securities and other interest-earning assets, less rates paid on deposits and borrowings. The primary sources of noninterest income are revenue from loan sales and servicing and fees from financial services provided to customers. A summary of the Company's key financial results are presented below:

The Company recorded a net loss for 2007 of \$67 million, or \$0.12 per diluted share, compared with net income of \$3.56 billion, or \$3.64 per diluted share, in 2006. The decline was primarily the result of significant credit deterioration in the Company's single-family residential mortgage loan portfolio and significant disruptions in the capital markets, including a sudden and severe contraction in secondary mortgage market liquidity for nonconforming residential loan products. These conditions also

contributed to the impairment of all goodwill associated with the Company's Home Loans business near the end of 2007.

Reflecting the significant credit deterioration, the Company recorded a provision for loan losses of \$3.11 billion in 2007, an increase of \$2.29 billion from 2006 and about twice the level of 2007 net charge-offs, which totaled \$1.62 billion. Adverse trends in key housing market indicators, including growing inventories of unsold homes, rising foreclosure rates and a significant contraction in the availability of credit for nonconforming mortgage products continued to deteriorate throughout 2007 and exerted significant downward pressure on home prices, particularly in areas of the country in which the Company's lending activities have been concentrated. Nationwide sales volume of existing homes in December 2007 was 22% lower than in December 2006, leading to a supply of unsold homes of approximately 9.7 months, a 47% increase from December 2006, while the national median sales price for existing homes declined by 7% between those same periods. Housing market weakness was also evident from the change in the national volume of foreclosure filings, which increased by 75% in 2007 compared with 2006. With the downturn in the housing market, single-family residential mortgage delinquency levels have increased substantially and loss severity rates have grown significantly. These conditions are reflected in the Company's nonperforming assets to total assets ratio, which increased from 0.80% at December 31, 2006 to 2.17% at December 31, 2007. Net mortgage loan charge-offs as a percentage of the average balance of the real estate loan portfolio increased from 0.09% in 2006 to 0.55% in 2007, and on an annualized basis, from 0.14% in the fourth quarter of 2006 to 1.08% in the fourth quarter of 2007, reflecting the accelerating pace of deterioration in the credit quality of the mortgage loan portfolio. The increase in loss severity rates was particularly evident in the subprime mortgage channel and home equity loans and lines of credit portfolios. With early indicators in 2008 suggesting that the housing market is continuing to deteriorate, the Company expects that it will experience significantly higher credit costs throughout its single-family residential mortgage portfolios.

Net credit card charge-offs as a percentage of the average balance of the credit card portfolio were 3.08% in 2006 and 3.69% in 2007, reflecting a gradual downturn in credit quality as the U.S. economy softened. The national unemployment rate, which held steady in a range of 4.4% to 4.7% for most of 2007, increased to 4.9% in January 2008, while average net job growth for the three months ending January 31, 2008 was 42,000, compared with 121,000 for the three months ending January 31, 2007. The Company expects net credit card charge-off rates will continue to rise if the economy is pressured further by higher unemployment levels and sluggish job growth.

Noninterest income was \$6.04 billion in 2007, compared with \$6.38 billion in 2006. Deteriorating credit conditions also caused significant disruptions in the secondary mortgage market, which adversely affected the Company's noninterest income results. Gain from home mortgage loans and originated mortgage-backed securities, net of hedging and risk management instruments, totaled \$59 million in 2007, compared with \$735 million in 2006. Credit quality concerns created uncertainty in the market for subprime mortgage products during the first half of 2007. Those concerns intensified during the second half of the year and spread into the broader secondary market, resulting in a severe contraction of secondary market liquidity as investors avoided purchasing all mortgage products backed by nonconforming loan collateral. Because of this disruption, the Company transferred approximately \$17 billion of real estate loans to its loan portfolio in the third quarter of 2007, representing substantially all of the Company's nonconforming loans that had been designated as held for sale. Illiquid secondary market conditions also affected the valuations of the Company's trading assets, which are primarily comprised of interests retained from mortgage loan and credit card securitizations. Widening credit spreads on these retained interests were primarily responsible for the loss on trading assets of \$673 million in 2007, compared with a loss of \$154 million in 2006. The Company also recognized other-than-temporary impairment losses of \$375 million in the available-for-sale securities portfolio during the second half of 2007 on certain mortgage-backed securities.

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Partially offsetting the losses in noninterest income were gains from mortgage servicing rights ("MSR") valuation and risk management of \$205 million in 2007, compared with a loss of \$393 million in 2006, as gains from the Company's MSR risk management instruments outpaced the decline in MSR fair value. While lower mortgage interest rates during the latter part of 2007 increased expected loan prepayment speeds, their effect on the MSR value was softened by the weakening housing market and the severe contraction in home mortgage credit availability, both of which significantly reduced home loan refinancing volume.

Noninterest expense totaled \$10.60 billion in 2007, compared with \$8.81 billion in 2006. The unprecedented challenges in the mortgage and credit markets during 2007 also had a significant effect on the Company's noninterest expense results. Noninterest expense in 2007 includes the fourth quarter effects from a \$1.78 billion pre-tax impairment loss related to all goodwill associated with the Home Loans business. This non-cash charge did not affect the Company's tangible equity or regulatory capital ratios, or its liquidity position. With the fundamental shift in the mortgage market from credit disruptions and the expectation of a prolonged period of secondary mortgage market illiquidity, the Company took actions in the fourth quarter of 2007 to resize its home loans business in anticipation of continued declines in loan volume within the home mortgage industry, and to accelerate the direction of the home loans business to mortgage lending conducted through the Company's retail banking stores and other retail distribution channels. Among the actions taken by the Company were:

Discontinuing all remaining lending through the subprime mortgage channel;

Initiating the closure of WaMu Capital Corp., the Company's institutional broker-dealer business;

Winding-down the Company's mortgage banker finance warehouse lending operations;

Eliminating approximately 2,600 positions in the Home Loans business and approximately 550 corporate and other support positions; and

Closing various home loan centers, sales offices, and home loan processing and call centers.

The Company recorded \$143 million of additional noninterest expense in the fourth quarter of 2007 as a result of these actions, which are expected to generate approximately \$500 million of expense savings during 2008.

Net interest income on a taxable-equivalent basis was \$8.19 billion in 2007, compared with \$8.13 billion in 2006. The increase was due to the expansion of the net interest margin, which increased, on a taxable-equivalent basis, from 2.60% in 2006 to 2.86% in 2007. The increase in the margin was primarily due to increases in the yields of mortgage loan products tied to short-term interest rate indices and the sales of lower-yielding mortgage loans. With the increasing deterioration in the housing market and the general softening of the economy, the Federal Reserve reduced the target Federal Funds rate by 100 basis points during the second half of 2007, and lowered this benchmark rate by another 125 basis points in January 2008, bringing the target rate down to 3.00%. As the Company's wholesale borrowing rates are usually correlated with interest rate policy changes made by the Federal Reserve and reprice to current market levels faster than most of the Company's interest-earning assets, the actions taken by the Fed are expected to further expand the margin in 2008.

To bolster its capital levels and liquidity position, the Company issued a total of \$3.9 billion of Tier 1 capital in the fourth quarter of 2007, comprised of \$2.9 billion, net, of noncumulative, perpetual convertible preferred stock issued by the Parent and \$1 billion of noncumulative, perpetual preferred shares issued by Washington Mutual Preferred Funding LLC, an indirect subsidiary of Washington Mutual Bank. Additionally, commencing in the first quarter of 2008, the Company reduced its quarterly cash dividend rate on the Company's common stock to 15 cents per share. At December 31, 2007, the Company's estimated total risk-based capital to total risk-weighted assets ratio was 12.34% and its

estimated Tier 1 capital to average total assets ratio was 6.84%, exceeding the minimum regulatory guidelines of 8% and 4%, respectively, while the Company's tangible equity to total tangible assets ratio was 6.67%, well above its established target of 5.50%.

### **Critical Accounting Estimates**

The preparation of financial statements in accordance with the accounting principles generally accepted in the United States of America ("GAAP") requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expenses in the financial statements. Various elements of the Company's accounting policies, by their nature, involve the application of highly sensitive and judgmental estimates and assumptions. Some of these policies and estimates relate to matters that are highly complex and contain inherent uncertainties. It is possible that, in some instances, different estimates and assumptions could reasonably have been made and used by management, instead of those the Company applied, which might have produced different results that could have had a material effect on the financial statements.

The Company has identified four accounting estimates that, due to the judgments and assumptions inherent in those estimates, and the potential sensitivity of its financial statements to those judgments and assumptions, are critical to an understanding of its financial statements. These estimates are: the fair value of certain financial instruments and other assets; the allowance for loan losses and contingent credit risk liabilities; other-than-temporary impairment losses on available-for-sale securities; and the determination of whether a derivative qualifies for hedge accounting.

Management has discussed the development and selection of these critical accounting estimates with the Audit Committee of the Company's Board of Directors. The Company believes that the judgments, estimates and assumptions used in the preparation of its financial statements are appropriate given the facts and circumstances as of December 31, 2007. The nature of these judgments, estimates and assumptions are described in greater detail in subsequent sections of Management's Discussion and Analysis and in Note 1 to the Consolidated Financial Statements "Summary of Significant Accounting Policies."

The discussion below presents information about the nature of the Company's critical accounting estimates:

#### **Fair Value of Certain Financial Instruments and Other Assets**

A portion of the Company's assets are carried at fair value, including: mortgage servicing rights, trading assets including certain retained interests from securitization activities, available-for-sale securities and derivatives. In addition, loans held for sale are recorded at the lower of cost or fair value. Changes in fair value of those instruments that qualify as hedged items under fair value hedge accounting are recognized in earnings and offset the changes in fair value of derivatives used as hedge accounting instruments.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Generally, for assets that are reported at fair value, the Company uses quoted market prices or internal valuation models to estimate their fair value. These models incorporate inputs such as forward yield curves, loan prepayment assumptions, market volatilities and pricing spreads utilizing market-based inputs where readily available. The degree of management judgment involved in estimating the fair value of a financial instrument or other asset is dependent upon the availability of quoted market prices or observable market value inputs. For financial instruments that are actively traded in the marketplace or whose values are based on readily available market value data, little judgment is necessary when estimating the instrument's fair value. When observable market prices and data are not readily



available, significant management judgment often is necessary to estimate fair value. In those cases, different assumptions could result in significant changes in valuation.

During the latter half of 2007, deteriorating credit conditions caused significant disruptions in the secondary mortgage market. Credit quality concerns prompted market participants to avoid purchasing mortgage investment products backed by nonconforming loan collateral. As market activity slowed, the availability of observable market prices was reduced. Accordingly, there was less market data available for use by management in the judgments applied to key valuation inputs.

The following financial instruments and other assets require the Company's most complex judgments and assumptions when estimating fair value:

*Mortgage Servicing Rights and Certain Other Retained Interests in Securitizations*

In June 2007, the Company implemented a model that is based on an option-adjusted spread ("OAS") valuation methodology to estimate the fair value of substantially all of its MSR asset. The model projects cash flows over multiple interest rate scenarios and discounts these cash flows using risk-adjusted discount rates. Additionally, an independent broker estimate of the fair values of the mortgage servicing rights is obtained quarterly along with other market-based evidence. Management uses this information together with its OAS valuation methodology to estimate the fair value of the MSR. Models used to value MSR assets, including those employing an OAS valuation methodology, are highly sensitive to changes in certain assumptions. Different expected prepayment speeds, in particular, can result in substantial changes in the estimated fair value of MSR. If actual prepayment experience differs materially from the expected prepayment speeds used in the Company's model, this difference may result in a material change in MSR fair value.

Changes in MSR value are reported in the Consolidated Statements of Income under the noninterest income caption "Revenue from sales and servicing of home mortgage loans." Additional discussion regarding the estimation of MSR fair value, including limitations to the MSR fair value measurement process, are described in the subsequent section of Management's Discussion and Analysis "Earnings Performance from Continuing Operations." Key economic assumptions and the sensitivity of MSR fair value to immediate changes in those assumptions are described in Note 8 to the Consolidated Financial Statements "Mortgage Banking Activities."

For other retained interests in securitization activities (such as interest-only strips and residual interests in mortgage and credit card securitizations), the discounted cash flow model used in estimating fair value utilizes projections of expected cash flows that are greatly influenced by expected prepayment speeds and, in some cases, expected net credit losses or finance charges related to the securitized assets. Key economic assumptions and the sensitivity of retained interests fair value to immediate changes in those assumptions are described in Note 7 to the Consolidated Financial Statements "Securitizations." Changes in those and other assumptions used could have a significant effect on the valuation of these retained interests. Changes in the value of other retained interests in securitization activities are reported in the Consolidated Statements of Income under the noninterest income caption "Loss on trading assets" and in the Consolidated Statements of Financial Condition as "Trading assets."

*Loans held for sale*

The fair value of loans designated as held-for-sale is generally based on observable market prices of securities that have loan collateral or interests in loans that are similar to the held-for-sale loans or whole loan sale prices if formally committed. If market prices are not readily available, fair value is based on a discounted cash flow model, which considers expected prepayment factors and the degree of credit risk associated with the loans and the estimated effects of changes in market interest rates relative to the loans' interest rates. When the estimated fair value of loans held for sale is lower than

their cost, including adjustments to cost if the loans were in a fair value hedge relationship under Financial Accounting Standards Board ("FASB") Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended ("Statement No. 133"), a valuation adjustment that accounts for this difference is reported in the Consolidated Statements of Income as a component within the noninterest income caption "Revenue from sales and servicing of home mortgage loans" for home loans. Valuation adjustments for consumer loans held for sale are recorded under the noninterest income caption "Revenue from sales and servicing of consumer loans." Valuation adjustments for multi-family and commercial real estate loans held for sale are recorded under the noninterest income caption "Other income."

#### *Fair Value of Reporting Units and Goodwill Impairment*

Under FASB Statement No. 142, *Goodwill and Other Intangible Assets*, goodwill must be allocated to reporting units and tested for impairment. The Company tests goodwill for impairment at least annually or more frequently if events or circumstances, such as adverse changes in the business, indicate that there may be justification for conducting an interim test. Impairment testing is performed at the reporting unit level (which is the same level as the Company's four major operating segments identified in Note 26 to the Consolidated Financial Statements "Operating Segments"). The first part of the test is a comparison, at the reporting unit level, of the fair value of each reporting unit to its carrying value, including goodwill. If the fair value is less than the carrying value, then the second part of the test is needed to measure the amount of potential goodwill impairment. The implied fair value of the reporting unit goodwill is calculated and compared with the actual carrying value of goodwill recorded within the reporting unit. If the carrying value of reporting unit goodwill exceeds the implied fair value of that goodwill, then the Company would recognize an impairment loss for the amount of the difference, which would be recorded as a charge against net income.

The fair value of the reporting units are determined primarily using discounted cash flow models based on each reporting unit's internal forecasts. In addition, analysis using market-based trading and transaction multiples, where available, is used to assess the reasonableness of the valuations derived from the discounted cash flow models.

For additional information regarding the carrying values of goodwill by operating segment, see Note 9 to the Consolidated Financial Statements "Goodwill and Other Intangible Assets."

#### **Allowance for Loan Losses and Contingent Credit Risk Liabilities**

##### *Allowance for Loan Losses*

The allowance for loan losses represents management's estimate of incurred credit losses inherent in the Company's loan portfolio as of the balance sheet date. Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for loan losses in future periods.

The estimate of the allowance is based on a variety of factors, including past loan loss experience, the current credit profile of borrowers, adverse situations that have occurred that may affect a borrower's ability to meet his financial obligations, the estimated value of underlying collateral, general economic conditions, and the impact that changes in interest rates and unemployment levels have on a borrower's ability to repay adjustable-rate loans.

The Company allocates a portion of the allowance to the homogeneous loan portfolios and estimates this allocated portion using statistical estimation techniques. Loss estimation techniques used in statistical models are supplemented by qualitative information to assist in estimating the allocated allowance. When housing prices are volatile, lags in data collection and reporting increase the likelihood of adjustments being made to the allowance.

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The Company also estimates an unallocated portion of the allowance that reflects management's assessment of various risk factors that are not fully captured by the statistical estimation techniques used to determine the allocated component of the allowance. The following factors are routinely and regularly reviewed in estimating the appropriateness of the unallocated allowance: national and local economic trends and conditions (such as gross domestic product and unemployment trends); market conditions (such as changes in housing prices); industry and borrower concentrations within portfolio segments (including concentrations by metropolitan statistical area); recent loan portfolio performance (such as changes in the levels and trends in delinquencies and impaired loans); trends in loan growth (including the velocity of change in loan growth); changes in underwriting criteria; and the regulatory and public policy environment.

The allowance for loan losses is reported in the Consolidated Statements of Financial Condition and the provision for loan losses is reported in the Consolidated Statements of Income.

The estimates and judgments are described in further detail in the subsequent section of Management's Discussion and Analysis "Credit Risk Management" and in Note 1 to the Consolidated Financial Statements "Summary of Significant Accounting Policies."

### *Contingent Credit Risk Liabilities*

In the ordinary course of business, the Company sells loans to third parties and in certain circumstances, such as in the event of early or first payment default, retains credit risk exposure on those loans. The Company may also be required to repurchase sold loans when representations and warranties made by the Company in connection with those sales are breached. Under certain circumstances, such as when a loan sold to an investor and serviced by the Company fails to perform according to its contractual terms within the six months after its origination or upon written request of the investor, the Company will review the loan file to determine whether or not errors may have been made in the process of originating the loan. If errors are discovered and it is determined that such errors constitute a violation of a representation or warranty made to the investor in connection with the Company's sale of the loan, then the Company will be required to either repurchase the loan or indemnify the investor for losses sustained if the violation had a material adverse effect on the value of the loan.

Reserves are established for the Company's exposure to the potential repurchase or indemnification liabilities described above as such liabilities are initially recorded at fair value. Throughout the life of these repurchase or indemnification liabilities, the Company may learn of additional information that can affect the assessment of loss probability or the estimation of the amounts involved. Changes in these assessments can lead to significant changes in the recorded reserves. Repurchase and indemnification liabilities are recorded within other liabilities in the Consolidated Statements of Financial Condition, and losses are recorded in the Consolidated Statements of Income under the noninterest income caption "Revenue from sales and servicing of home mortgage loans."

### **Impairment of Securities**

The Company monitors securities in its available-for-sale investment portfolio for impairment. Impairment may result from credit deterioration of the issuer, from changes in market rates relative to the interest rate of the instrument, or from changes in prepayment speeds. The Company considers many factors in determining whether the impairment is other than temporary, including but not limited to adverse changes in expected cash flows, the length of time the security has had a fair value less than the cost basis, the severity of the unrealized loss, the Company's intent and ability to hold the security for a period of time sufficient for a recovery in value and issuer-specific factors such as the issuer's financial condition, external credit ratings and general market conditions. The determination of

other-than-temporary impairment is a subjective process, requiring the use of judgments and assumptions in interpreting relevant market data. Other-than-temporary valuation losses on available-for-sale securities are reported in the Consolidated Statements of Income under the noninterest income caption "Loss on other available-for-sale securities." For additional information regarding the amortized cost, unrealized gains, unrealized losses, and fair value of securities, see Note 5 to the Consolidated Financial Statements "Available-for-Sale Securities."

### **Derivatives and Hedging Activities**

The Company enters into derivative contracts to manage the various risks associated with certain assets, liabilities, or probable forecasted transactions. When the Company enters into derivative contracts, the derivative instrument is designated as: (1) a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment (a "fair value" hedge); (2) a hedge of the variability in expected future cash flows associated with an existing recognized asset or liability or a probable forecasted transaction (a "cash flow" hedge); or (3) held for other risk management purposes ("risk management derivatives").

All derivatives, whether designated in hedging relationships or not, are recorded at fair value as either assets or liabilities in the Consolidated Statements of Financial Condition. Changes in fair value of derivatives that are not in hedge accounting relationships (as in (3) above) are recorded in the Consolidated Statements of Income in the period in which the change in value occurs. Changes in the fair value of derivatives that are designated as cash flow hedges (as in (2) above), to the extent such hedges are deemed highly effective, are recorded as a separate component of accumulated other comprehensive income and reclassified into earnings when the earnings effect of the hedged cash flows is recognized. Changes in the fair value of derivatives in qualifying fair value hedge accounting relationships (as in (1) above) are recorded each period in earnings along with the change in fair value of the hedged item attributable to the risk being hedged.

The determination of whether a derivative qualifies for hedge accounting requires complex judgments about the application of Statement No. 133. Additionally, this Statement requires contemporaneous documentation of the Company's hedge relationships. Such documentation includes the nature of the risk being hedged, the identification of the hedged item, or the group of hedged items that share the risk exposure that is designated as being hedged, the selection of the instrument that will be used to hedge the identified risk, and the method used to assess the effectiveness of the hedge relationship. The assessment of hedge effectiveness requires calculations that utilize standard statistical methods of correlation that must support the determination that the hedging relationship is expected to be highly effective, during the period that the hedge is designated, in achieving offsetting changes in fair value or cash flows attributable to the hedged risk. If the Company's assessment of effectiveness is not considered to be adequate to achieve hedge accounting treatment, the derivative is treated as a free-standing risk management instrument.

### **Recently Issued Accounting Standards Not Yet Adopted**

Refer to Note 1 to the Consolidated Financial Statements "Summary of Significant Accounting Policies."

### **Discontinued Operations**

In December 2006, the Company exited the retail mutual fund management business and completed the sale of WM Advisors, Inc. WM Advisors provided investment management, distribution and shareholder services to the WM Group of Funds. This former subsidiary has been accounted for as a discontinued operation and, accordingly, its results of operations have been removed from the Company's results of continuing operations for the years ended December 31, 2006 and 2005 in the

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Consolidated Statements of Income and in Note 26 to the Consolidated Financial Statements "Operating Segments."

**Five-Year Summary of Selected Financial Data**

	December 31,				
	2007	2006	2005	2004	2003
(in millions, except per share amounts)					
<b>Income Statement Data</b> (for the year ended)					
Net interest income	\$ 8,177	\$ 8,121	\$ 8,218	\$ 7,411	\$ 7,865
Provision for loan losses	3,107	816	316	209	42
Noninterest income	6,042	6,377	5,097	4,061	5,437
Noninterest expense	10,600	8,807	7,620	7,332	7,267
Net income (loss)	(67)	3,558	3,432	2,878	3,880
Basic earnings per common share:					
Income (loss) from continuing operations	(0.11)	3.27	3.80	2.84	4.17
Income from discontinued operations		0.47	0.04	0.50	0.12
Net income (loss)	(0.11)	3.74	3.84	3.34	4.29
Diluted earnings per common share:					
Income (loss) from continuing operations	(0.12)	3.18	3.69	2.77	4.09
Income from discontinued operations		0.46	0.04	0.49	0.12
Net income (loss)	(0.12)	3.64	3.73	3.26	4.21
Dividends declared per common share	2.21	2.06	1.90	1.74	1.40
<b>Balance Sheet Data</b> (at year end)					
Available-for-sale securities	\$ 27,540	\$ 24,978	\$ 24,659	\$ 19,219	\$ 36,707
Loans held for sale	5,403	44,970	33,582	42,743	20,837
Loans held in portfolio	244,386	224,960	229,632	207,071	175,150
Mortgage servicing rights	6,278	6,193	8,041	5,906	6,354
Goodwill	7,287	9,050	8,298	6,196	6,196
Total assets	327,913	346,288	343,573	307,581	275,178
Total deposits	181,926	213,956	193,167	173,658	153,181
Securities sold under agreements to repurchase	4,148	11,953	15,532	15,944	28,333
Advances from Federal Home Loan Banks	63,852	44,297	68,771	70,074	48,330
Other borrowings	38,958	32,852	23,777	18,498	15,483
Minority interests	3,919	2,448	15	13	
Stockholders' equity	24,584	26,969	27,279	20,889	19,405
<b>Supplemental Data</b>					
Loan volume:					
Home loans:					
Adjustable-rate	\$ 70,324	\$ 110,914	\$ 125,758	\$ 128,263	\$ 113,677
Fixed-rate	30,554	47,469	81,964	84,099	270,504
Total home loan volume	100,878	158,383	207,722	212,362	384,181
Total loan volume	151,502	205,085	260,770	266,397	431,906

**Ratios and Other Supplemental Data**

	Year Ended December 31,		
	2007	2006	2005
	(dollars in millions, except per share amounts)		
<b>Profitability</b>			
Return on average assets	(0.02)%	1.02%	1.05%
Return on average common equity	(0.42)	13.52	14.91
Net interest margin	2.85	2.60	2.79
Efficiency ratio <sup>(1)(2)</sup>	74.55	60.75	57.23
<b>Asset Quality</b> (at year end)			
Nonaccrual loans	\$ 6,123	\$ 2,295	\$ 1,686
Foreclosed assets	979	480	276
Total nonperforming assets <sup>(3)</sup>	7,102	2,775	1,962
Nonperforming assets <sup>(3)</sup> to total assets	2.17%	0.80%	0.57%
Allowance for loan losses	\$ 2,571	\$ 1,630	\$ 1,695
Allowance as a percentage of total loans held in portfolio	1.05%	0.72%	0.74%
<b>Credit Performance</b>			
Net charge-offs	\$ 1,623	\$ 510	\$ 244
<b>Capital Adequacy</b> (at year end)			
Stockholders' equity to total assets	7.50%	7.79%	7.94%
Tangible equity to total tangible assets <sup>(4)</sup>	6.67	6.04	5.62
Tier 1 capital to average total assets (leverage) <sup>(5)</sup>	6.84	6.35	5.83
Total risk-based capital to total risk-weighted assets <sup>(5)</sup>	12.34	11.77	10.80
<b>Per Common Share Data</b>			
Common shares outstanding at the end of period (in thousands) <sup>(6)</sup>	869,036	944,479	993,914
Common stock dividend payout ratio	N/M	55.08%	49.48%
Book value per common share (at year end) <sup>(7)</sup>	\$ 24.55	\$ 28.21	\$ 27.61
Market prices:			
High	45.56	46.48	44.54
Low	13.07	41.47	36.92
Year end	13.61	45.49	43.50

N/M = Not meaningful

- (1) Based on continuing operations.
- (2) The efficiency ratio is defined as noninterest expense divided by total revenue (net interest income and noninterest income).
- (3) Excludes nonaccrual loans held for sale.
- (4) Excludes unrealized net gain/loss on available-for-sale securities and cash flow hedging instruments, goodwill and intangible assets (except MSR) and the impact from the adoption and application of FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*. Minority interests of \$3.92 billion for December 31, 2007 and \$2.45 billion for December 31, 2006 are included in the numerator.
- (5) The capital ratios are estimated as if Washington Mutual, Inc. were a bank holding company subject to Federal Reserve Board capital requirements.
- (6) Includes six million shares held in escrow.
- (7) Excludes six million shares held in escrow.

**Earnings Performance from Continuing Operations**

Average balances, together with the total dollar amounts of interest income and expense related to such balances and the weighted average rates, were as follows:

	Year Ended December 31,								
	2007			2006			2005		
	Average Balance	Rate	Interest Income/Expense	Average Balance	Rate	Interest Income/Expense	Average Balance	Rate	Interest Income/Expense
(dollars in millions)									
<b>Assets<sup>(1)</sup></b>									
Interest-earning assets <sup>(2)</sup> :									
Federal funds sold and securities purchased under agreements to resell	\$ 3,475	5.31%	\$ 184	\$ 4,718	5.20%	\$ 245	\$ 2,154	3.42%	\$ 74
Trading assets	4,546	9.45	430	7,829	7.74	606	7,217	6.50	469
Available-for-sale securities <sup>(3)</sup> :									
Mortgage-backed securities	19,647	5.49	1,078	21,534	5.41	1,165	16,359	4.81	786
Investment securities	7,334	5.13	377	5,992	4.92	295	4,494	4.71	212
Loans held for sale	20,421	6.81	1,391	27,791	6.50	1,807	44,847	5.34	2,394
Loans held in portfolio <sup>(4)</sup> :									
Loans secured by real estate:									
Home loans <sup>(5)(6)</sup>	98,547	6.49	6,396	120,320	5.83	7,011	110,326	4.97	5,485
Home equity loans and lines of credit <sup>(6)</sup>	56,285	7.46	4,197	52,265	7.33	3,833	47,909	6.01	2,878
Subprime mortgage channel <sup>(7)</sup>	20,125	6.62	1,333	20,202	6.31	1,275	20,561	5.90	1,214
Home construction <sup>(8)</sup>	2,074	6.79	141	2,061	6.46	133	2,074	6.22	129
Multi-family	30,162	6.59	1,988	27,386	6.28	1,721	24,070	5.41	1,303
Other real estate	7,504	6.98	524	5,797	6.93	402	5,091	7.11	362
<b>Total loans secured by real estate</b>	<b>214,697</b>	<b>6.79</b>	<b>14,579</b>	<b>228,031</b>	<b>6.30</b>	<b>14,375</b>	<b>210,031</b>	<b>5.41</b>	<b>11,371</b>
Consumer:									
Credit card	10,113	10.55	1,067	8,733	11.19	977	2,082	11.96	249
Other	242	13.90	34	444	11.12	50	707	10.67	75
Commercial	1,916	8.10	155	1,886	6.94	131	2,614	5.04	132
<b>Total loans held in portfolio</b>	<b>226,968</b>	<b>6.98</b>	<b>15,835</b>	<b>239,094</b>	<b>6.50</b>	<b>15,533</b>	<b>215,434</b>	<b>5.49</b>	<b>11,827</b>
Other	4,275	4.53	194	5,220	4.90	256	4,324	3.65	158
<b>Total interest-earning assets</b>	<b>286,666</b>	<b>6.80</b>	<b>19,489</b>	<b>312,178</b>	<b>6.38</b>	<b>19,907</b>	<b>294,829</b>	<b>5.40</b>	<b>15,920</b>
Noninterest-earning assets:									
Mortgage servicing rights	6,616			7,667			6,597		
Goodwill	9,018			8,489			6,712		
Other assets	21,089			20,424			18,095		
<b>Total assets</b>	<b>\$ 323,389</b>			<b>\$ 348,758</b>			<b>\$ 326,233</b>		
<b>Liabilities<sup>(1)</sup></b>									
Interest-bearing liabilities:									
Deposits:									
Interest-bearing checking deposits	\$ 29,261	2.42	709	\$ 36,477	2.63	960	\$ 46,524	1.95	906
Savings and money market deposits	56,459	3.27	1,846	48,866	2.96	1,446	42,555	1.76	750
Time deposits	82,551	4.91	4,055	84,106	4.59	3,857	62,175	3.33	2,072
<b>Total interest-bearing deposits</b>	<b>168,271</b>	<b>3.93</b>	<b>6,610</b>	<b>169,449</b>	<b>3.70</b>	<b>6,263</b>	<b>151,254</b>	<b>2.46</b>	<b>3,728</b>
Federal funds purchased and commercial paper	3,096	5.30	164	7,347	5.06	371	5,314	3.56	190
Securities sold under agreements to repurchase	8,330	5.32	443	15,257	5.12	781	15,365	3.40	523

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Year Ended December 31,

Advances from Federal Home Loan Banks	37,144	5.28	1,963	56,619	4.99	2,828	68,713	3.46	2,377
Other	38,157	5.59	2,132	28,796	5.36	1,543	21,603	4.09	884
<b>Total interest-bearing liabilities</b>	<b>254,998</b>	<b>4.44</b>	<b>11,312</b>	<b>277,468</b>	<b>4.25</b>	<b>11,786</b>	<b>262,249</b>	<b>2.94</b>	<b>7,702</b>
Noninterest-bearing sources:									
Noninterest-bearing deposits	32,109			34,380			34,769		
Other liabilities	9,155			8,865			6,177		
Minority interests	2,933			1,639			14		
Stockholders' equity	24,194			26,406			23,024		
<b>Total liabilities and stockholders' equity</b>	<b>\$ 323,389</b>			<b>\$ 348,758</b>			<b>\$ 326,233</b>		
Net interest spread and net interest income		2.36	\$ 8,177		2.13	\$ 8,121		2.46	\$ 8,218
Impact of noninterest-bearing sources		0.49			0.47			0.33	
Net interest margin		2.85			2.60			2.79	
<b>Taxable-Equivalent Basis</b>									
Net interest margin and net interest income on a taxable-equivalent basis <sup>(9)</sup>		2.86	\$ 8,191		2.60	\$ 8,129		2.79	\$ 8,225



- (1) Average balances of assets and liabilities of acquired companies are calculated by dividing the stub period of the Company's ownership of those assets or liabilities by one year.
- (2) Nonaccrual assets and related income, if any, are included in their respective categories.
- (3) The average balance and yield are based on average amortized cost balances.
- (4) Interest income for loans held in portfolio includes amortization of net deferred loan origination costs of \$391 million, \$463 million, and \$402 million for the years ended December 31, 2007, 2006 and 2005.
- (5) Capitalized interest recognized in earnings that resulted from negative amortization within the Option ARM portfolio totaled \$1.42 billion, \$1.07 billion, and \$292 million for the years ended December 31, 2007, 2006 and 2005.
- (6) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (7) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (8) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.
- (9) Includes taxable-equivalent adjustments primarily related to tax-exempt income on U.S. states and political subdivisions securities and loans related to the Company's community lending and investment activities. The federal statutory tax rate was 35% for the periods presented.

The dollar amounts of interest income and interest expense fluctuate depending upon changes in interest rates and upon changes in the volume of interest-earning assets and interest-bearing liabilities. Changes attributable to (i) changes in volume (changes in average outstanding balances multiplied by the prior period's rate), (ii) changes in rate (changes in average interest rates multiplied by the prior period's volume), and (iii) changes in rate/volume (changes in rate multiplied by the change in volume)

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which were allocated in proportion to the percentage changes in average volume and average rate and included in the relevant column below were as follows:

	2007 vs. 2006			2006 vs. 2005		
	Increase/(Decrease) Due to		Total Change	Increase/(Decrease) Due to		Total Change
	Volume	Rate		Volume	Rate	
(in millions)						
<b>Interest Income</b>						
Federal funds sold and securities purchased under agreements to resell	\$ (66)	\$ 5	\$ (61)	\$ 119	\$ 52	\$ 171
Trading assets	(291)	115	(176)	42	95	137
Available-for-sale securities:						
Mortgage-backed securities	(104)	17	(87)	271	108	379
Investment securities	69	13	82	73	10	83
Loans held for sale	(499)	83	(416)	(1,036)	449	(587)
Loans held in portfolio:						
Loans secured by real estate:						
Home loans <sup>(1)</sup>	(1,357)	742	(615)	526	1,000	1,526
Home equity loans and lines of credit <sup>(1)</sup>	299	65	364	279	676	955
Subprime mortgage channel <sup>(2)</sup>	(5)	63	58	(22)	83	61
Home construction <sup>(3)</sup>	1	7	8	(1)	5	4
Multi-family	180	87	267	193	225	418
Other real estate	119	3	122	49	(9)	40
Total loans secured by real estate	(763)	967	204	1,024	1,980	3,004
Consumer:						
Credit card	148	(58)	90	745	(17)	728
Other	(26)	10	(16)	(29)	4	(25)
Commercial	2	22	24	(42)	41	(1)
Total loans held in portfolio	(639)	941	302	1,698	2,008	3,706
Other	(44)	(18)	(62)	37	61	98
Total interest income	(1,574)	1,156	(418)	1,204	2,783	3,987
<b>Interest Expense</b>						
Deposits:						
Interest-bearing checking deposits	(179)	(72)	(251)	(222)	276	54
Savings and money markets deposits	239	161	400	125	571	696
Time deposits	(73)	271	198	864	921	1,785
Total deposits	(13)	360	347	767	1,768	2,535
Federal funds purchased and commercial paper	(224)	17	(207)	87	94	181
Securities sold under agreements to repurchase	(368)	30	(338)	(4)	262	258
Advances from Federal Home Loan Banks	(1,021)	156	(865)	(471)	922	451
Other	520	69	589	342	317	659
Total interest expense	(1,106)	632	(474)	721	3,363	4,084
Net interest income	\$ (468)	\$ 524	\$ 56	\$ 483	\$ (580)	\$ (97)

(1)

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- (2) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (2) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (3) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.

**Net Interest Income**

Net interest income and the net interest margin, both expressed on a taxable-equivalent basis, totaled \$8.19 billion and 2.86% in 2007, compared with \$8.13 billion and 2.60% in 2006. The increase in the net interest margin was primarily due to increases in the yields of mortgage loan products tied to short-term interest rate indices and the sales of lower-yielding mortgage loans, and a favorable change in the mix between deposits and comparatively higher cost borrowed funds. Deposits funded 70% of the interest-earning asset base during 2007, compared with 65% in 2006. A decline in average interest earning assets in 2007 partially offset the expansion of the margin, as the Company sought to deemphasize balance sheet growth during a time in which the yield curve was relatively flat or slightly inverted.

**Noninterest Income**

Noninterest income from continuing operations consisted of the following:

	Year Ended December 31,			Percentage Change	
	2007	2006	2005	2007/2006	2006/2005
	(in millions)				
Revenue from sales and servicing of home mortgage loans	\$ 944	\$ 768	\$ 2,017	23%	(62)%
Revenue from sales and servicing of consumer loans	1,639	1,527	413	7	270
Depositor and other retail banking fees	2,893	2,567	2,193	13	17
Credit card fees	778	637	139	22	358
Securities fees and commissions	260	215	189	21	13
Insurance income	116	127	172	(8)	(26)
Loss on trading assets	(673)	(154)	(257)	336	(40)
Loss on other available-for-sale securities	(319)	(9)	(84)		(90)
Other income	404	699	315	(42)	122
Total noninterest income	\$ 6,042	\$ 6,377	\$ 5,097	(5)	25

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Revenue from sales and servicing of home mortgage loans

Revenue from sales and servicing of home mortgage loans, including the effects of derivative risk management instruments, consisted of the following:

	Year Ended December 31,			Percentage Change	
	2007	2006	2005	2007/2006	2006/2005
	(in millions)				
Revenue from sales and servicing of home mortgage loans:					
Sales activity:					
Gain from home mortgage loans and originated mortgage-backed securities <sup>(1)</sup>	\$ 52	\$ 626	\$ 873	(92)%	(28)%
Revaluation gain from derivatives economically hedging loans held for sale	7	109	76	(93)	42
Gain from home mortgage loans and originated mortgage-backed securities, net of hedging and risk management instruments	59	735	949	(92)	(23)
Servicing activity:					
Home mortgage loan servicing revenue <sup>(2)</sup>	2,047	2,181	2,110	(6)	3
Change in MSR fair value due to payments on loans and other <sup>(3)</sup>	(1,363)	(1,654)		(18)	
Change in MSR fair value due to valuation inputs or assumptions <sup>(3)</sup>	(157)	299			
MSR valuation adjustments <sup>(4)</sup>			965		
Amortization of MSR			(2,170)		
Revaluation gain (loss) from derivatives economically hedging MSR	358	(636)	163		
Adjustment to MSR fair value for MSR sale		(157)			
Home mortgage loan servicing revenue, net of MSR valuation changes and derivative risk management instruments	885	33	1,068		(97)
Total revenue from sales and servicing of home mortgage loans	\$ 944	\$ 768	\$ 2,017	23	(62)

- (1) Originated mortgage-backed securities represent available-for-sale securities retained on the balance sheet subsequent to the securitization of mortgage loans that were originated by the Company.
- (2) Includes contractually specified servicing fees (net of guarantee fees paid to housing government-sponsored enterprises, where applicable), late charges and loan pool expenses (the shortfall of the scheduled interest required to be remitted to investors and that which is collected from borrowers upon payoff).
- (3) Line item descriptions reflect the impact of the adoption of Statement No. 156 on January 1, 2006. The retrospective application of this statement to prior periods is not permitted.
- (4) Net of fair value hedge ineffectiveness as well as any impairment/reversal recognized on MSR that resulted from the application of the lower of cost or fair value accounting methodology in 2005.

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The following table presents MSR valuation and the corresponding risk management derivative instruments and securities during the years ended December 31, 2007 and 2006:

	Year Ended December 31,	
	2007	2006
(in millions)		
<b>MSR Valuation and Risk Management:</b>		
Change in MSR fair value due to valuation inputs or assumptions	\$ (157)	\$ 299
<b>Gain (loss) on MSR risk management instruments:</b>		
Revaluation gain (loss) from derivatives	358	(636)
Revaluation gain (loss) from certain trading securities	4	(55)
Loss from certain available-for-sale securities		(1)
<b>Total gain (loss) on MSR risk management instruments</b>	<b>362</b>	<b>(692)</b>
<b>Total changes in MSR valuation and risk management</b>	<b>\$ 205</b>	<b>\$ (393)</b>

The following tables reconcile the gains (losses) on investment securities that are designated as MSR risk management instruments to loss on trading assets and loss on other available-for-sale securities that are reported within noninterest income during the years ended December 31, 2007 and 2006:

	Year Ended December 31,	
	2007	2006
(in millions)		
<b>Gain (loss) on trading assets resulting from:</b>		
MSR risk management instruments	\$ 4	\$ (55)
Other	(677)	(99)
<b>Total loss on trading assets</b>	<b>\$ (673)</b>	<b>\$ (154)</b>

	Year Ended December 31,	
	2007	2006
(in millions)		
<b>Loss on other available-for-sale securities resulting from:</b>		
MSR risk management instruments	\$	\$ (1)
Other	(319)	(8)
<b>Total loss on other available-for-sale securities</b>	<b>\$ (319)</b>	<b>\$ (9)</b>

Gain from home mortgage loans and originated mortgage-backed securities, net of hedging and risk management instruments was \$59 million in 2007, compared with \$735 million in the prior year. Secondary market conditions for subprime mortgage loans rapidly deteriorated during the first half of 2007 in response to the weakening housing market. As credit risk concerns from rising subprime mortgage borrower defaults increased, credit spreads widened to reflect secondary market demands for higher risk premiums on subprime mortgage loans, which lowered the value of the loans to be sold. Credit concerns spread across the secondary market in the second half of 2007 as mortgage delinquencies and loss severities across all single-family residential borrower classes accelerated. This led to a severe contraction in risk tolerances among secondary market participants and resulted in an illiquid market for nonconforming home loans. With the absence of liquidity

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for such loans, home loan sales volume totaled only \$17.38 billion in the last half of 2007, a 69% decline from \$56.58 billion for the same period in 2006. The Company transferred into its held for investment portfolio approximately

\$15 billion of single-family residential loans in the third quarter of 2007, which were substantially comprised of nonconforming products that had initially been designated as held for sale prior to the rapid contraction in secondary market liquidity. A \$139 million downward adjustment on the transferred loans was recorded based on the lower of cost or fair value, reflecting the wider secondary market credit spreads that accompanied the market disruption.

The fair value changes in home mortgage loans held for sale and the offsetting changes in the derivative instruments used as fair value hedges are recorded within gain from home mortgage loans when hedge accounting treatment is achieved. Home mortgage loans held for sale where hedge accounting treatment is not achieved are recorded at the lower of cost or fair value. This accounting method requires declines in the fair value of these loans, to the extent such value is below their cost basis, to be immediately recognized within gain from home mortgage loans, but any increases in the value of these loans that exceed their original cost basis may not be recorded until the loans are sold. However, all changes in the value of derivative instruments that are used to manage the interest rate risk of these loans must be recognized in earnings as those changes occur.

In March 2006, the FASB issued Statement No. 156, *Accounting for Servicing of Financial Assets*, which amends Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, permitting for the first time an entity to report classes of servicing assets at fair value at each reporting date and to record changes in fair value of such reported classes of servicing assets in earnings in the period in which the changes occur. The Company applied Statement No. 156 to its financial statements on January 1, 2006 and elected to measure its mortgage servicing assets at fair value. Upon electing the fair value method of accounting for its mortgage servicing assets, the Company discontinued the application of fair value hedge accounting. Accordingly, beginning in 2006, all derivatives held for MSR risk management are treated as economic hedges, with valuation changes recorded as revaluation gain (loss) from derivatives economically hedging MSR. Additionally, upon the change from the lower of cost or fair value accounting method to fair value accounting under Statement No. 156, the calculation of amortization and the assessment of impairment were discontinued and the MSR valuation allowance was written off against the recorded value of the MSR. Those measurements have been replaced by fair value adjustments that encompass market-driven valuation changes and the runoff in value that occurs as scheduled loan payments are made over time, which are each separately reported.

Home mortgage loan servicing revenue decreased by \$134 million for the year ended December 31, 2007, compared with 2006. The decrease was largely the result of the sale of \$2.53 billion of mortgage servicing rights in July 2006. The decline was more than offset by a decrease in the rate of MSR fair value changes from loan payments of \$291 million between the same years, as actual payment rates on the servicing portfolio decreased in 2007 due to significantly lower levels of refinancing activity.

MSR valuation and risk management results were a gain of \$205 million in 2007, compared with a loss of \$393 million in 2006. Although mortgage interest rates at the end of 2007 were at similar levels to those that existed at the beginning of the year, more significant fluctuations occurred over the course of 2007, which led to a modest decrease in MSR value of \$157 million for the year. The decrease in value occurred primarily during the second half of 2007, as mortgage rates generally declined during that period, resulting in higher expected prepayment speeds. However, the impact of lower interest rates on projected MSR prepayment speeds was mitigated by a smaller increase in expected prepayment rates, reflecting diminished opportunities for borrowers to refinance during a period when the housing market is weakening, underwriting standards across the mortgage banking industry have tightened and rates for nonconforming loan products are higher. The performance of the MSR risk management instruments was adversely affected by the flat-to-inverted slope of the yield curve in 2006, which had the effect of increasing hedging costs.



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The value of the MSR asset is subject to prepayment risk. Future expected net cash flows from servicing a loan in the servicing portfolio will not be realized if the loan pays off earlier than expected. Moreover, since most loans within the servicing portfolio do not impose prepayment fees for early payoff, a corresponding economic benefit will not be received if the loan pays off earlier than expected. The fair value of the MSR is estimated from the present value of the future net cash flows the Company expects to receive from the servicing portfolio. Accordingly, prepayment risk subjects the MSR to potential declines in fair value. During the second quarter of 2007, the Company adopted an option-adjusted spread ("OAS") valuation methodology for estimating the fair value of substantially all of its MSR asset. This methodology projects MSR cash flows over multiple interest rate scenarios, and discounts those cash flows using risk-adjusted discount rates to arrive at an estimate of the fair value of the MSR asset. As the Company's OAS model was calibrated to the prior model's valuation results, the conversion to the new methodology did not result in a fair value adjustment to the Company's MSR asset upon its implementation.

### *All Other Noninterest Income Analysis*

Revenue from sales and servicing of consumer loans increased \$112 million for the year ended December 31, 2007, compared with 2006. While revenue from sales increased between the two periods as a result of a 50% increase in credit card securitization volume, revenue from servicing declined in 2007, when compared with 2006. This decline in servicing revenue was a result of realization of higher than originally estimated interest and fees charged on securitized loans and lower than originally estimated credit losses.

Depositor and other retail banking fees increased \$326 million for the year ended December 31, 2007, compared with 2006, predominantly due to higher transaction fees and an increase in the number of noninterest-bearing checking accounts. The number of noninterest-bearing checking accounts at December 31, 2007 totaled approximately 11.0 million compared with approximately 9.6 million at December 31, 2006.

Credit card fees increased \$141 million for the year ended December 31, 2007, compared with 2006, reflecting growth in the average balance of the credit card portfolio.

Securities fees and commissions increased \$45 million for the year ended December 31, 2007, compared with 2006, due to an increase in the volume of mutual fund and annuity sales.

Loss on trading assets increased \$519 million for the year ended December 31, 2007, compared with 2006. Similar to the way in which capital market disruptions affected the Company's mortgage banking results, the severe downturn in the housing market and rising levels of credit card delinquencies contributed to less favorable economic assumptions used to measure the value of trading assets retained from mortgage loan and credit card securitizations.

The Company recognizes impairment losses on available-for-sale securities through the income statement when it has concluded that a decrease in the fair value of a security is other than temporary. During the second half of 2007, the Company recognized charges totaling \$375 million related to mortgage-backed securities where it determined that a decline in fair value below amortized cost represented an other-than-temporary condition.

The decrease in other income of \$295 million for the year ended December 31, 2007, compared with 2006, primarily resulted from losses related to equity method investments and revaluation losses on derivatives held for risk management purposes. In addition, included in 2006 was a \$149 million litigation award from the partial settlement of the Company's claim against the U.S. Government with regard to the Home Savings supervisory goodwill lawsuit.

**Noninterest Expense**

Noninterest expense from continuing operations consisted of the following:

	Year Ended December 31,			Percentage Change	
	2007	2006	2005	2007/2006	2006/2005
	(in millions)				
Compensation and benefits	\$ 3,766	\$ 3,937	\$ 3,701	(4)%	6%
Occupancy and equipment	1,589	1,711	1,520	(7)	13
Telecommunications and outsourced information services	530	554	449	(4)	23
Depositor and other retail banking losses	262	229	226	14	2
Advertising and promotion	445	443	315		41
Professional fees	233	227	181	3	26
Postage	417	471	293	(12)	61
Foreclosed asset expense	309	117	75	164	56
Goodwill impairment charge	1,775				
Other expense	1,274	1,118	860	14	30
<b>Total noninterest expense</b>	<b>\$ 10,600</b>	<b>\$ 8,807</b>	<b>\$ 7,620</b>	<b>20</b>	<b>16</b>

Noninterest expense in 2007 includes the fourth quarter effects from a \$1.78 billion pre-tax impairment loss related to all goodwill associated with the Home Loans business. With the fundamental shift in the mortgage market from credit disruptions and the expectation of a prolonged period of secondary mortgage market illiquidity, the Company also recorded charges of \$143 million in the fourth quarter to resize its Home Loans business and corporate support functions in anticipation of continued declines in home mortgage industry loan originations, and to accelerate the direction of its mortgage banking operations to home lending conducted through retail banking stores and other retail distribution channels. The charges consist of \$58 million in employee termination benefits, \$42 million in lease termination and other decommissioning costs, and \$43 million of fixed asset write-downs.

The Company determined that the actions associated with the resizing of the Home Loans business represent restructuring activities. Accordingly, the resizing expenses described above included \$98 million of restructuring charges that resulted from the discontinuation of subprime mortgage lending, the announced closure of WaMu Capital Corp., the wind-down of the Company's mortgage banker finance operations, and the closure of certain home loans production centers and back-office support functions. The restructuring charges are described further in Note 2 to the Consolidated Financial Statements "Restructuring Activities."

Compensation and benefits expense decreased \$171 million, or 4%, from 2006, primarily due to lower home loan mortgage banking incentive compensation that resulted from the significant decline in home loan volume. The number of employees decreased from 49,824 employees at December 31, 2006 to 49,403 employees at December 31, 2007. Employee headcount was further reduced to 48,433 at January 31, 2008, reflecting the fourth quarter 2007 actions to resize the Company's Home Loans business and corporate support functions.

The decrease in occupancy and equipment expense during 2007 was primarily due to charges in 2006 of approximately \$185 million related to the Company's productivity and efficiency initiatives, partially offset by charges in 2007 to resize the Company's Home Loans business and corporate support functions.

Depositor and other retail banking losses increased during 2007 predominantly due to an increase in the number of transaction accounts, resulting in an increase in loss levels for returned deposited items and overdrawn account losses.

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Postage expense decreased during 2007 due to a decline in courier expense related to improved efficiency in the cash distribution process in the Company's retail banking operations.

The increase in foreclosed asset expense during 2007 was due to higher foreclosures reflecting the deterioration in the credit environment and further weakening in the housing market. The total number of foreclosed properties has increased while the values of those properties have generally declined.

The increase in other expense from 2006 was partly due to charges of \$88 million for Visa related litigation liabilities recognized during 2007. The Company recognized charges of \$38 million in the third quarter of 2007 related to its share of the American Express settlement of a covered litigation matter and \$50 million in the fourth quarter of 2007 to accrue for a contingent obligation for certain unresolved disputes involving Visa and its members.

### Income Taxes

For 2007, a tax provision of \$376 million was recorded, compared with a tax provision of \$1.66 billion for 2006. The tax provision recorded for 2007 was significantly impacted by the pre-tax goodwill impairment charge of \$1.78 billion, of which approximately \$1.3 billion is not deductible for income tax purposes. The effective tax rate for the tax benefit recorded on the goodwill impairment charge was 9.83%. Excluding the goodwill impairment charge, the effective tax rate for 2007 would have been 26.41%, compared with 34.73% in 2006. The reduction in the effective tax rate for 2007 (excluding the goodwill impairment charge) is mostly due to reduced income from continuing operations before income taxes.

### Review of Financial Condition

#### Trading Assets

Trading assets consisted of the following:

	December 31,	
	2007	2006
	(in millions)	
Credit card retained interests	\$ 1,838	\$ 1,464
Mortgage-backed securities	854	2,880
U.S. Government and other debt securities	76	90
Total trading assets	\$ 2,768	\$ 4,434

The Company's trading assets are primarily comprised of financial instruments that are retained from securitization transactions. Credit card retained interests are mostly comprised of subordinated interests that consist of noninterest bearing beneficial interests. These retained interests are repaid after the related senior classes of securities, which are usually held by third party investors.

Trading assets at December 31, 2007 decreased \$1.67 billion from December 31, 2006 predominantly due to a \$1.85 billion decline in securities held by WaMu Capital Corp. ("WCC"), an indirect subsidiary of the Company. During December 2007, the Company announced its intention to close WCC, its institutional broker-dealer business, as part of restructuring its Home Loans business.

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The following table presents trading assets, including mortgage-backed securities by asset type, by investment grade at December 31, 2007:

	AAA <sup>(1)</sup>	AA	A	BBB	Below Investment Grade	Total
(in millions)						
Credit card retained interests	\$	\$ 34	\$ 108	\$ 284	\$ 1,412	\$ 1,838
Mortgage-backed securities:						
Agency		53				53
Prime		310	5	32	39	409
Alt-A		116	89	37	34	321
Subprime					2	20 <sup>(2)</sup>
Commercial					49	49
Total mortgage-backed securities		479	94	69	75	854
U.S. Government and other debt securities		76				76
Total trading assets	\$	\$ 555	\$ 128	\$ 177	\$ 359	\$ 1,549
						\$ 2,768

(1) Includes securities guaranteed by the U.S. Government or U.S. Government sponsored agencies, which are not rated.

(2) Represents retained interest in subprime mortgage loan securitizations, including \$5 million in residual interests.

**Available-for-Sale Securities**

Available-for-sale securities consisted of the following:

	December 31,	
	2007	2006
(in millions)		
Available-for-sale securities, total amortized cost of \$27,789 and \$25,073:		
Mortgage-backed securities	\$ 19,249	\$ 18,601
Investment securities	8,291	6,377
Total available-for-sale securities	\$ 27,540	\$ 24,978

The Company holds available-for-sale securities primarily for interest rate risk management and liquidity enhancement purposes. Accordingly, the portfolio is comprised primarily of highly-rated debt securities.

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The fair value of available-for-sale mortgage-backed securities by asset type and investment grade at December 31, 2007 is presented in the following table:

	AAA <sup>(1)</sup>	AA	A	BBB	Below Investment Grade	Total
(in millions)						
<b>Mortgage-backed securities:</b>						
Agency	\$ 7,192	\$	\$	\$	\$	\$ 7,192
Prime	3,801	540	161	73		4,575
Alt-A	600	175	68	74	23	940
Subprime	236	88	121	37	9	491
Commercial	6,015	17		10	9	6,051
<b>Total mortgage-backed securities</b>	<b>\$ 17,844</b>	<b>\$ 820</b>	<b>\$ 350</b>	<b>\$ 194</b>	<b>\$ 41</b>	<b>\$ 19,249</b>

(1) Includes securities guaranteed by the U.S. Government or U.S. Government sponsored agencies, which are not rated.

At December 31, 2007, available-for-sale investment securities were comprised primarily of U.S. Government-sponsored agency securities and securities issued by U.S. states and political subdivisions. Substantially all investment securities are investment grade.

Refer to Note 5 to the Consolidated Financial Statements "Available-for-Sale Securities" for additional information on securities, classified by security type.

**Loans**

Total loans consisted of the following:

	December 31,				
	2007	2006	2005	2004	2003
(in millions)					
<b>Loans held for sale</b>	<b>\$ 5,403</b>	<b>\$ 44,970</b>	<b>\$ 33,582</b>	<b>\$ 42,743</b>	<b>\$ 20,837</b>
<b>Loans held in portfolio:</b>					
<b>Loans secured by real estate:</b>					
Home loans <sup>(1)</sup>	\$ 110,387	\$ 99,479	\$ 114,144	\$ 109,950	\$ 100,043
Home equity loans and lines of credit <sup>(1)</sup>	60,963	52,882	50,840	43,648	27,644
<b>Subprime mortgage channel<sup>(2)</sup>:</b>					
Home loans	16,092	18,725	21,146	19,184	12,973
Home equity loans and lines of credit	2,525	2,042	11	2	3
Home construction <sup>(3)</sup>	2,226	2,082	2,037	2,344	2,220
Multi-family <sup>(4)</sup>	31,754	30,161	25,601	22,282	20,324
Other real estate <sup>(5)</sup>	9,524	6,745	5,035	5,664	6,649
<b>Total loans secured by real estate</b>	<b>233,471</b>	<b>212,116</b>	<b>218,814</b>	<b>203,074</b>	<b>169,856</b>
<b>Consumer:</b>					
Credit card	8,831	10,861	8,043		
Other	205	276	638	792	1,028
Commercial	1,879	1,707	2,137	3,205	4,266

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December 31,

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Total loans held in portfolio <sup>(6)</sup>	\$ 244,386	\$ 224,960	\$ 229,632	\$ 207,071	\$ 175,150

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(1) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.

(2) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.

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- (3) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.
- (4) Includes multi-family construction balances of \$967 million, \$740 million, \$632 million, \$333 million and \$325 million at December 31, 2007, 2006, 2005, 2004 and 2003.
- (5) Includes other commercial real estate construction balances of \$812 million, \$414 million, \$208 million, \$277 million and \$382 million at December 31, 2007, 2006, 2005, 2004 and 2003.
- (6) Includes net unamortized deferred loan costs of \$1.45 billion, \$1.88 billion, \$1.96 billion, \$1.87 billion and \$1.55 billion at December 31, 2007, 2006, 2005, 2004 and 2003.

Due to the illiquid market, residential mortgage loans designated as held for sale at December 31, 2007 were largely limited to conforming loans eligible for purchase by the housing government-sponsored enterprises. The December 31, 2006 balance of loans held for sale included approximately \$17.5 billion of medium-term adjustable-rate home loans which were transferred during the fourth quarter of 2006 from loans held in portfolio to loans held for sale. These loans were subsequently sold during the first quarter of 2007. In addition, as a result of the severe contraction in secondary market liquidity, the Company transferred approximately \$17 billion of real estate loans to its loan portfolio during the third quarter of 2007, which represented substantially all of the Company's nonconforming loans that had been designated as held for sale prior to the market disruption.

Total home loans held in portfolio consisted of the following:

	<b>December 31,</b>	
	<b>2007</b>	<b>2006</b>
	<b>(in millions)</b>	
<b>Home loans:</b>		
Short-term adjustable-rate loans <sup>(1)</sup> :		
Option ARMs <sup>(2)</sup>	\$ 58,870	\$ 63,557
Other ARMs	9,551	6,791
	68,421	70,348
Total short-term adjustable-rate loans		
Medium-term adjustable-rate loans <sup>(3)</sup>	36,507	26,232
Fixed-rate loans	5,459	2,899
	110,387	99,479
Home loans held in portfolio <sup>(4)</sup>		
Subprime mortgage channel	16,092	18,725
	126,479	118,204
Total home loans held in portfolio	\$ 126,479	\$ 118,204

- (1) Short-term adjustable-rate loans reprice within one year.
- (2) The total amount by which the unpaid principal balance of Option ARM loans exceeded their original principal amount was \$1.73 billion and \$888 million at December 31, 2007 and 2006.
- (3) Medium-term adjustable-rate loans reprice after one year.
- (4) Excludes home loans in the subprime mortgage channel.

The home loans held in portfolio balance at December 31, 2007 increased \$8.28 billion from December 31, 2006. The increase was due primarily to the transfer of approximately \$15 billion of nonconforming home loans previously designated as loans held for sale prior to the market disruption experienced during the third quarter of 2007. Partially offsetting this increase was a decrease in Option ARM loans, reflecting the slowdown in the housing market and an interest rate environment in which loan products with longer repricing frequencies are priced more favorably than short-term adjustable-rate loans.

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The balance of home equity loans and lines of credit at December 31, 2007, excluding home equity loans and lines of credit in the subprime mortgage channel, increased 15% from December 31, 2006 primarily due to growth in lines of credit.



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Home, multi-family and other commercial real estate construction loans and commercial business loans by maturity date were as follows:

	December 31, 2007			
	Due Within One Year	After One But Within Five Years	After Five Years	Total
(in millions)				
<b>Home construction<sup>(1)</sup>:</b>				
Adjustable-rate	\$ 1,021	\$ 154	\$ 217	\$ 1,392
Fixed-rate	108	3	723	834
<b>Multi-family construction:</b>				
Adjustable-rate	248	413	11	672
Fixed-rate	148	31	116	295
<b>Other commercial real estate construction:</b>				
Adjustable-rate	313	476	1	790
Fixed-rate			22	22
<b>Commercial business:</b>				
Adjustable-rate	1,320	101	148	1,569
Fixed-rate	92	151	67	310
<b>Total</b>	<b>\$ 3,250</b>	<b>\$ 1,329</b>	<b>\$ 1,305</b>	<b>\$ 5,884</b>

(1) Includes \$37 million of loans to builders and \$2.19 billion of loans to the intended occupant of a single-family residence.

**Deposits**

Deposits consisted of the following:

	December 31,	
	2007	2006
(in millions)		
<b>Retail deposits:</b>		
<b>Checking deposits:</b>		
Noninterest bearing	\$ 23,476	\$ 22,838
Interest bearing	25,713	32,723
<b>Total checking deposits</b>	<b>49,189</b>	<b>55,561</b>
Savings and money market deposits	44,987	41,943
Time deposits	49,410	46,821
<b>Total retail deposits</b>	<b>143,586</b>	<b>144,325</b>
Commercial business and other deposits	11,267	15,175
<b>Brokered deposits:</b>		
Consumer	18,089	22,299
Institutional	2,515	22,339
Custodial and escrow deposits	6,469	9,818
<b>Total deposits</b>	<b>\$ 181,926</b>	<b>\$ 213,956</b>

December 31,

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Interest-bearing retail checking deposits decreased as customers shifted from Platinum checking accounts to time deposits and savings and money market deposits as a result of higher interest rates offered for these products.

Institutional brokered deposits decreased \$19.82 billion or 89% from December 31, 2006, largely due to reduced funding needs as the Company reduced total assets approximately 10% during the first

half of 2007. During the second half of 2007, as a result of the illiquid capital markets, the Company retained nonconforming mortgage loan products in its portfolio. The increase in assets was funded with more readily available and lower cost funding sources such as advances from FHLBs. Advances from FHLBs increased from \$44.30 billion at December 31, 2006 to \$63.85 billion at December 31, 2007.

Transaction accounts (checking, savings and money market deposits) comprised 66% of retail deposits at December 31, 2007 and 68% at December 31, 2006. These products generally have the benefit of lower interest costs, compared with time deposits, and represent the core customer relationship that is maintained within the retail banking franchise. Average total deposits funded 70% of average total interest-earning assets for the year ended December 31, 2007, compared with 65% for the year ended December 31, 2006.

### **Operating Segments**

The Company has four operating segments for the purpose of management reporting: the Retail Banking Group, the Card Services Group, the Commercial Group and the Home Loans Group. The Company's operating segments are defined by the products and services they offer. The Retail Banking Group, the Card Services Group and the Home Loans Group are consumer-oriented while the Commercial Group serves commercial customers. In addition, the category of Corporate Support/Treasury and Other includes the community lending and investment operations; the Treasury function, which manages the Company's interest rate risk, liquidity position and capital; the Corporate Support function, which provides facilities, legal, accounting and finance, human resources and technology services; and the Enterprise Risk Management function, which oversees the identification, measurement, monitoring, control and reporting of credit, market and operational risk.

The Company serves the needs of 19.8 million consumer households through its 2,257 retail banking stores, 233 lending stores and centers, 4,713 owned and branded ATMs, telephone call centers and online banking.

The principal activities of the **Retail Banking Group** include: (1) offering a comprehensive line of deposit and other retail banking products and services to consumers and small businesses; (2) holding the substantial majority of the Company's held for investment portfolios of home loans, home equity loans and home equity lines of credit (but not the Company's held for investment portfolios of home loans, home equity loans and home equity lines of credit made to higher risk borrowers through the subprime mortgage channel); (3) originating home equity loans and lines of credit; and (4) providing investment advisory and brokerage services, sales of annuities and other financial services.

Deposit products offered to consumers and small businesses include the Company's signature free checking and interest-bearing Platinum checking accounts, as well as other personal checking, savings, money market deposit and time deposit accounts. Many products are offered in retail banking stores and online. Financial consultants provide investment advisory and securities brokerage services to the public.

On December 31, 2006, the Company sold its retail mutual fund management business, WM Advisors, Inc. The results of operations of WM Advisors for the years ended December 31, 2006 and 2005 are reported within the Retail Banking Group's results as discontinued operations and the gain on disposition of these discontinued operations, net of certain transaction expenses, is reported in the Corporate Support/Treasury and Other category.

The **Card Services Group** manages the Company's credit card operations. The segment's principal activities include: (1) issuing credit cards; (2) either holding outstanding balances on credit cards in portfolio or securitizing and selling them; (3) servicing credit card accounts; and (4) providing other cardholder services. Credit card balances that are held in the Company's loan portfolio generate interest income from finance charges on outstanding card balances, and noninterest income from the

collection of fees associated with the credit card portfolio, such as performance fees (late, overlimit and returned check charges) and cash advance and balance transfer fees.

The Card Services Group acquires new customers primarily by leveraging the Company's retail banking distribution network and through direct mail solicitations, augmented by online and telemarketing activities and other marketing programs including affinity programs. In addition to credit cards, this segment markets a variety of other products to its customer base.

The Company evaluates the performance of the Card Services Group on a managed asset basis. Managed financial information is derived by adjusting the GAAP financial information to add back securitized loan balances and the related interest, fee income and provision for credit losses.

The principal activities of the **Commercial Group** include: (1) providing financing to developers and investors, or acquiring loans for the purchase or refinancing of multi-family dwellings and other commercial properties; (2) either holding multi-family and other commercial real estate loans in portfolio or selling these loans while retaining the servicing rights; and (3) providing deposit services to commercial customers.

The principal activities of the **Home Loans Group** include: (1) the origination, fulfillment and servicing of home loans; (2) the origination, fulfillment and servicing of home equity loans and lines of credit; (3) managing the Company's capital markets operations, which includes the buying and selling of all types of real estate secured loans in the secondary market; and (4) holding the Company's held for investment portfolios of home loans, home equity loans and home equity lines of credit made to higher risk borrowers through the subprime mortgage channel.

During the fourth quarter of 2007, the Company announced that, in response to a fundamental shift in the home mortgage market due to credit dislocation and a prolonged period of reduced capital markets liquidity, it significantly changed the strategic focus of its Home Loans business to accelerate its alignment with the Company's retail banking operations. As part of these restructuring activities, the Company discontinued all remaining lending through its subprime mortgage channel, closed approximately 200 home loan locations, including 190 home loan centers and sales offices and nine home loans processing and call centers, eliminated approximately 2,600 positions in the Home Loans business, initiated the closure of WaMu Capital Corp., its institutional broker-dealer business, and began winding-down its mortgage banker finance warehouse lending operation.

The segment offers a wide variety of real estate secured residential loan products and services. Such loans are held in portfolio by the Home Loans Group, sold to secondary market participants or transferred through inter-segment sales to the Retail Banking Group. During the second half of 2007, loans that historically had been transferred to the held for investment portfolio within the Retail Banking Group were retained within the held for investment portfolio within the Home Loans Group. The decision to retain or sell loans, and the related decision to retain or not retain servicing when loans are sold, involves the analysis and comparison of expected interest income and the interest rate and credit risks inherent with holding loans in portfolio, with the expected servicing fees, the size of the gain or loss that would be realized if the loans were sold and the expected expense of managing the risk related to any retained mortgage servicing rights.

The principal activities of, and charges reported in, the **Corporate Support/Treasury and Other** category include:

management of the Company's interest rate risk, liquidity position and capital. These responsibilities involve managing a majority of the Company's portfolio of investment securities and providing oversight and direction across the enterprise over matters that impact the profile of the Company's balance sheet. Such matters include determining the optimal product composition of loans that the Company holds in portfolio, the appropriate mix of wholesale and

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capital markets borrowings at any given point in time and the allocation of capital resources to the business segments;

enterprise-wide management of the identification, measurement, monitoring, control and reporting of credit, market and operational risk;

community lending and investment activities, which help fund the development of affordable housing units in traditionally underserved communities;

general corporate overhead costs associated with the Company's facilities, legal, accounting and finance functions, human resources and technology services;

costs that the Company's chief operating decision maker did not consider when evaluating the performance of the Company's four operating segments, including: (1) costs associated with the Company's productivity and efficiency initiatives; (2) costs related to the partial MSR sale in 2006; and (3) gain on the disposition of discontinued operations;

the impact of changes in the unallocated allowance for loan losses;

the net impact of funds transfer pricing for loan and deposit balances; and

items associated with transfers of loans from the Retail Banking Group to the Home Loans Group when home loans previously designated as held for investment are transferred to held for sale, such as lower of cost or fair value adjustments and the write-off of the inter-segment profit factor.

The Company uses various **management accounting methodologies**, which are enhanced from time to time, to assign certain balance sheet and income statement items to the responsible operating segment. Unlike financial accounting, there is no comprehensive, authoritative guidance for management accounting. The management accounting process measures performance based on the management structure of the Company and is not necessarily comparable with similar information for any other financial institution. Methodologies that are applied to the measurement of segment profitability include:

a funds transfer pricing system, which allocates interest income funding credits and funding charges between the operating segments and the Treasury Division. A segment will receive a funding credit from the Treasury Division for its liabilities and its share of risk-adjusted economic capital. Conversely, a segment is assigned a charge by the Treasury Division to fund its assets. The system takes into account the interest rate risk profile of the Company's assets and liabilities and concentrates their sensitivities within the Treasury Division, where the risk profile is centrally managed. Certain basis and other residual risks are managed and reported in the operating segments;

the allocation of charges for services rendered to certain segments by functions centralized within another segment, as well as the allocation of certain operating expenses that are not directly charged to the segments (i.e., corporate overhead), which generally are based on each segment's consumption patterns;

the allocation of goodwill and other intangible assets to the operating segments based on benefits received from each acquisition;

the accounting for inter-segment transactions, which include the transfer from the Home Loans Group to the Retail Banking Group of certain originated home and home equity loans that are to be held in portfolio and a revenue arrangement between Home Loans and Retail Banking. When originated home and home equity loans are transferred to the Retail Banking Group, the Home Loans Group records a gain on the sale of the loans based on an assumed inter-segment profit factor. This profit factor is included in the book value of the transferred loans and is



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amortized as an adjustment to the net interest income recorded by the Retail Banking Group while the loan is held for investment. With the severe contraction in secondary mortgage market liquidity during the second half of 2007, the Company's chief operating decision maker determined that it was more relevant to measure the performance of the Home Loans Group without considering the assumed profit factor. Accordingly, home loans originated by the Home Loans Group during the second half of 2007 were retained within its portfolio, thereby not subjecting those loans to the inter-segment transfer profit factor. When a loan that was designated as held for investment within the Retail Banking Group is subsequently transferred to held for sale, the remaining inter-segment profit factor is written off through Corporate Support/Treasury and Other. When home loans initiated through retail banking stores are transferred to held for sale, the Retail Banking Group records a gain on sale of those loans based on an assumed inter-segment profit factor. The results of all inter-segment activities are eliminated as reconciling adjustments that are necessary to conform the presentation of management accounting policies to the accounting principles used in the Company's consolidated financial statements; and

a provisioning methodology that is consistent with that used in financial accounting.

Financial highlights by operating segments were as follows:

### Retail Banking Group

	Year Ended December 31,			Percentage Change	
	2007	2006	2005	2007/2006	2006/2005
(dollars in millions)					
<b>Condensed income statement:</b>					
Net interest income	\$ 5,142	\$ 5,201	\$ 4,893	(1)%	6%
Provision for loan losses	1,134	167	119	577	41
Noninterest income	3,254	2,914	2,575	12	13
Inter-segment revenue	48	58	42	(18)	39
Noninterest expense	4,567	4,364	4,177	5	4
<hr/>					
Income from continuing operations before income taxes	2,743	3,642	3,214	(25)	13
Income taxes	869	1,392	1,216	(38)	14
<hr/>					
Income from continuing operations	1,874	2,250	1,998	(17)	13
Income from discontinued operations		38	38		
<hr/>					
Net income	\$ 1,874	\$ 2,288	\$ 2,036	(18)	12

### Performance and other data:

Efficiency ratio	54.09%	53.39%	55.63%	1	(4)
Average loans	\$ 149,409	\$ 177,401	\$ 163,405	(16)	9
Average assets	159,184	187,735	173,631	(15)	8
Average deposits	144,233	140,344	136,893	3	3
Loan volume	18,926	20,354	32,953	(7)	(38)
Employees at end of period	28,784	27,629	32,751	4	(16)

The decrease in net interest income in 2007 was primarily due to a decline in the average balances of home mortgage loans. This decline reflects the transfer of approximately \$17.5 billion medium-term adjustable-rate portfolio home loans in the fourth quarter of 2006 to held for sale in the Home Loans Group. The decline in average loans was also driven by the decision to retain home loans originated in the second half of 2007 by the Home Loans Group within that segment's portfolio. The decrease in net interest income was partially offset by a \$3.89 billion growth in average deposits.

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The substantial increase in the provision for loan losses in 2007 was the result of increased delinquencies from the deteriorating housing market and the subsequent impact on losses in the portfolio.

The increase in noninterest income in 2007 was substantially due to a 13% increase in depositor and other retail banking fees, reflecting the strong growth in the number of noninterest-bearing checking accounts and higher transaction fees. The number of noninterest-bearing retail checking accounts at December 31, 2007 totaled approximately 11.0 million, compared with approximately 9.6 million at December 31, 2006. Noninterest income for the year ended December 31, 2006 included a \$21 million incentive payment received as part of the Company's migration of its debit card business to MasterCard.

Noninterest expense increased primarily due to higher compensation and benefits expense and occupancy and equipment expense within the retail banking franchise. Compensation and benefits expense increased due to higher performance-based incentive compensation and a 4% increase in headcount related to the opening of 32 net new retail banking stores in 2007. Included in noninterest expense for 2007 was foreclosed asset expense of \$60 million.

### Card Services Group (Managed basis)

	<u>Year Ended December 31,</u>		<u>October 1, 2005 (Acquisition Date) through December 31, 2005</u>	<u>Percentage Change</u>
	<u>2007</u>	<u>2006</u>		<u>2007/2006</u>
(dollars in millions)				
<b>Condensed income statement:</b>				
Net interest income	\$ 2,659	\$ 2,496	\$ 642	7%
Provision for loan losses	2,113	1,647	454	28
Noninterest income	1,581	1,528	352	4
Noninterest expense	1,337	1,205	275	11
	<u>790</u>	<u>1,172</u>	<u>265</u>	
Income before income taxes				(33)
Income taxes	250	448	100	(44)
	<u>540</u>	<u>724</u>	<u>165</u>	
Net income				(25)

### Performance and other data:

Efficiency ratio	31.53%	29.96%	27.63%	5
Average loans	\$ 25,066	\$ 21,294	\$ 4,908	18
Average assets	27,502	23,888	5,595	15
Employees at end of period	2,860	2,611	3,124	10

The Company evaluates the performance of the Card Services Group on a managed basis. Managed financial information is derived by adjusting the GAAP financial information to add back securitized loan balances and the related interest, fee income and provision for credit losses.

The increase in net interest income in 2007 was substantially due to higher average balances of managed credit card loans, which increased \$3.77 billion from 2006. The increase was partially offset by lower yields, reflecting the decrease in the prime interest rate and a shift to retail accounts which have a narrower spread.



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The increase in the provision for loan losses reflects the increase in balances of managed credit card loans and the softening of the economy resulting in increases in delinquencies and lower levels of anticipated recoveries.

The increase in noninterest income during 2007 was substantially due to increased gain on securitizations due to a higher volume of securitizations and higher fee income. The increase was substantially offset by market valuation losses resulting from changes in performance assumptions and the disruption in the capital markets.

Noninterest expense increased largely from charges of \$88 million for Visa related litigation liabilities.

### Commercial Group

	Year Ended December 31,			Percentage Change	
	2007	2006	2005	2007/2006	2006/2005
(dollars in millions)					
<b>Condensed income statement:</b>					
Net interest income	\$ 820	\$ 719	\$ 758	14%	(5)%
Provision for loan losses	24	(82)	(26)		218
Noninterest income	35	99	200	(65)	(50)
Noninterest expense	282	259	243	9	7
Income before income taxes	549	641	741	(14)	(14)
Income taxes	174	245	279	(29)	(12)
Net income	\$ 375	\$ 396	\$ 462	(5)	(14)
<b>Performance and other data:</b>					
Efficiency ratio	32.93%	31.68%	25.32%	4	25
Average loans	\$ 38,975	\$ 33,230	\$ 30,308	17	10
Average assets	41,296	35,565	33,351	16	7
Average deposits	12,722	10,364	7,796	23	33
Loan volume	16,873	12,854	11,231	31	14
Employees at end of period	1,406	1,416	1,325	(1)	7

The increase in net interest income in 2007 was primarily due to increased interest income on higher average balances of multi-family and non-residential real estate loans. Average loan balances reflect the acquisition of Commercial Capital Bancorp on October 1, 2006.

The increase in the provision for loan losses during 2007 was primarily due to growth in loan balances. The provision in 2006 included a \$60 million reduction in the allowance related to refinements in the Company's estimate of the allowance attributable to multi-family loans.

A significant portion of the decrease in noninterest income in 2007 was due to losses on trading securities and lower gains on sale of multi-family and commercial loans, net of hedging and risk management instruments.

Noninterest expense in 2007 increased primarily due to the addition of Commercial Capital Bancorp and a 31% increase in loan volume.

## Home Loans Group

	Year Ended December 31,			Percentage Change	
	2007	2006	2005	2007/2006	2006/2005
(dollars in millions)					
<b>Condensed income statement:</b>					
Net interest income	\$ 878	\$ 1,165	\$ 1,966	(25)%	(41)%
Provision for loan losses	985	189	110	421	71
Noninterest income	1,061	1,296	2,425	(18)	(47)
Inter-segment expense	48	58	42	(18)	39
Noninterest expense	3,939	2,295	2,590	72	(11)
Income (loss) before income taxes	(3,033)	(81)	1,649		
Income taxes	(573)	(31)	622		
Net income (loss)	\$ (2,460)	\$ (50)	\$ 1,027		

**Performance and other data:**

Efficiency ratio	208.33%	95.48%	59.56%	118	60
Average loans	\$ 48,131	\$ 47,586	\$ 65,077	1	(27)
Average assets	64,695	72,772	87,422	(11)	(17)
Average deposits	7,836	11,535	14,114	(32)	(18)
Loan volume	115,241	171,569	216,308	(33)	(21)
Employees at end of period	11,323	12,934	17,651	(12)	(27)

The decrease in net interest income in 2007 was primarily due to the effect of transfer pricing on lower average balances of custodial deposits resulting from the \$2.53 billion sale of mortgage servicing rights in 2006. Also contributing to the decrease was higher transfer pricing charges on subprime loans and higher balances of loans held for investment, which have a lower spread than loans held for sale. Average balances of loans held for investment increased during the second half of 2007, when deteriorating credit conditions caused significant contraction in secondary market liquidity for nonconforming loans, resulting in the Company's decision to transfer approximately \$15 billion of such loans from held for sale and retain home loans originated by the Home Loans Group within the segment.

The increase in the provision for loan losses reflects the downturn in the housing market resulting in increased delinquencies and higher credit costs and the impact of the retention of home loans originated by the Home Loans Group within the segment during the second half of 2007.

The decrease in noninterest income in 2007 was primarily due to reduced gain on sale from an illiquid secondary market and decreased sales volume, including a reduced volume of loans sold to the Retail Banking Group, and an increase in trading losses on securities. Partially offsetting this decrease was increased income from MSR valuation and risk management activities and higher loan servicing income.

The increase in noninterest expense in 2007 was predominately due to a \$1.78 billion impairment loss recognized in the fourth quarter related to all of this segment's goodwill as a result of the fundamental shift in the mortgage market and the actions the Company is taking to resize its Home Loans business. The increase was partially offset by lower compensation and benefits expense resulting from a reduction in employee headcount. Included in noninterest expense for 2007 was foreclosed asset expense of \$245 million.

## Corporate Support/Treasury and Other

	Year Ended December 31,			Percentage Change	
	2007	2006	2005	2007/2006	2006/2005
(dollars in millions)					
<b>Condensed income statement:</b>					
Net interest income (expense)	\$ (86)	\$ (304)	\$ (105)	(72)%	190%
Provision for loan losses	51	(162)	(82)		98
Noninterest income (expense)	(137)	303	(171)		
Noninterest expense	475	684	335	(31)	104
Minority interest expense	203	105		93	
Loss from continuing operations before income taxes	(952)	(628)	(529)	52	19
Income taxes	(308)	(296)	(241)	4	23
Loss from continuing operations	(644)	(332)	(288)	94	15
Income from discontinued operations		406			
Net income (loss)	\$ (644)	\$ 74	\$ (288)		

**Performance and other data:**

Average loans	\$ 1,403	\$ 1,126	\$ 931	25	21
Average assets	44,651	40,722	30,143	10	35
Average deposits	35,589	41,586	27,220	(14)	53
Loan volume	462	308	278	50	11
Employees at end of period	5,030	5,234	5,947	(4)	(12)

The improvement in net interest income in 2007 was primarily due to lower interest expense on lower average balances of FHLB borrowings and wholesale deposits.

The decrease in noninterest income was primarily due to \$375 million of losses recognized in the second half of 2007 representing impairment on certain mortgage-backed securities where the reduction in fair value was deemed to be other than temporary. Noninterest income for the year ended December 31, 2006 included a litigation award of \$149 million from the partial settlement of the Home Savings supervisory goodwill lawsuit.

The decrease in noninterest expense in 2007 is primarily due to lower occupancy and equipment expense as a result of back office location consolidations in 2006 as well as lower compensation and benefits expense resulting from the Company's productivity and efficiency initiatives.

Minority interest expense represents dividends on preferred securities that were issued during 2006 and 2007 by Washington Mutual Preferred Funding LLC ("WMPF LLC"), an indirect subsidiary of Washington Mutual Bank. For further detail, refer to Note 17 to the Consolidated Financial Statements "Preferred Stock and Minority Interest."

On December 31, 2006, the Company completed the sale of WM Advisors, Inc., its retail mutual fund management business. The activities of WM Advisors, Inc. were reported within the Retail Banking Group as discontinued operations. The gain from the sale is included in income from discontinued operations in the Corporate Support/Treasury and Other category.

**Off-Balance Sheet Activities and Contractual Obligations****Asset Securitization**

The Company transforms loans into securities through a process known as securitization. When the Company securitizes loans, the loans are usually sold to a qualifying special-purpose entity ("QSPE"),



typically a trust. The QSPE, in turn, issues securities, commonly referred to as asset-backed securities, which are secured by future cash flows on the sold loans. The QSPE sells the securities to investors, which entitle the investors to receive specified cash flows during the term of the security. The QSPE uses the proceeds from the sale of these securities to pay the Company for the loans sold to the QSPE. These QSPEs are not consolidated within the financial statements since they satisfy the criteria established by Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. In general, these criteria require the QSPE to be legally isolated from the transferor (the Company), be limited to permitted activities, and have defined limits on the types of assets it can hold and the permitted sales, exchanges or distributions of its assets.

When the Company sells or securitizes loans that it originated, it generally retains the right to service the loans and may retain senior, subordinated, residual, and other interests, all of which are considered retained interests in the sold or securitized assets. Retained interests in mortgage loan securitizations, excluding the rights to service such loans, were \$1.71 billion at December 31, 2007, of which \$1.56 billion are of investment grade quality. Retained interests in credit card securitizations were \$1.84 billion at December 31, 2007, of which \$426 million are of investment grade quality. Additional information concerning securitization transactions is included in Notes 7 and 8 to the Consolidated Financial Statements "Securitizations" and "Mortgage Banking Activities."

#### *American Securitization Forum Framework*

On December 6, 2007, the American Securitization Forum ("ASF"), working with various constituency groups as well as representatives of U.S. federal government agencies, issued the Streamlined Foreclosure and Loss Avoidance Framework for Securitized Subprime Adjustable Rate Mortgage Loans (the "ASF Framework") to enable residential mortgage loan servicers to streamline their loss avoidance and loan modification practices. In adopting the ASF Framework, the ASF commented that current subprime residential mortgage market conditions reflect a number of concerns that impact securitization transactions, subprime mortgage lending and the overall housing market: an increase in delinquency, default and foreclosure rates; an increase in real estate owned inventories; a decline in home prices; and a prevalence of loans with relatively low initial fixed interest rates that are entering their adjustable rate periods at significantly higher interest rate levels. The ASF Framework provides guidance for residential mortgage loan servicers to streamline subprime residential mortgage borrower evaluation procedures and to facilitate the use of foreclosure avoidance and loss prevention efforts to reduce the number of such borrowers who might default during 2008 because they cannot afford to make higher monthly loan payments after their loans reset to a higher, adjustable interest rate.

The parameters of the ASF Framework were designed by the ASF to improve administrative efficiency while still maximizing cash flows to the QSPEs in which residential mortgage loans were transferred upon securitization by stratifying subprime borrowers into the following segments: borrowers that can refinance into readily available mortgage industry products ("Segment 1"); borrowers that have demonstrated the ability to pay their introductory rates, are unable to refinance, and are unable to afford their reset rates ("Segment 2"); and borrowers that require in-depth, case-by-case analysis due to loan histories that demonstrate difficulties in making timely, introductory rate payments ("Segment 3"). Consistent with its objectives, the ASF Framework was designed to fast-track loan modifications for Segment 2 borrowers, in which default is considered to be reasonably foreseeable. Under the ASF Framework, fast-track loan modifications would be available to Segment 2 borrowers with first-lien residential mortgage loans that: (1) have an initial fixed interest rate period of 36 months or less; (2) are included in securitized pools; (3) were originated between January 1, 2005 and July 31, 2007; and (4) have an initial interest rate reset date between January 1, 2008 and July 31, 2010. To be eligible for a fast-track loan modification under the ASF Framework, Segment 2 borrowers would also have to occupy the property as their primary residence and meet a specific FICO test, which is based on their current

FICO score, and the servicer must ascertain that the upcoming loan rate reset will result in an increase in the loan payment amount by more than 10%. If all of these criteria are satisfied, the servicer would be permitted to modify the Segment 2 borrower's loan interest rate by keeping it at the existing fixed interest rate, generally for five years following the upcoming reset period.

On January 8, 2008, the Securities and Exchange Commission's (the "SEC") Office of the Chief Accountant (the "OCA") issued a letter (the "OCA Letter") addressing accounting issues that may be raised by the ASF Framework. Specifically, the OCA Letter expressed the view that if a subprime loan made to a Segment 2 borrower is modified in accordance with the ASF Framework and that loan could be legally modified, the OCA would not object to continued status of the transferee as a QSPE under Statement No. 140.

As acknowledged in the OCA Letter, a uniform definition of a subprime mortgage loan does not exist within the mortgage banking industry. The Company has defined subprime residential mortgage loans by reference to the channel in which such loans were originated or purchased. Accordingly, the Company considers loans that were either originated under the Company's Long Beach Mortgage name or that were purchased from entities that are recognized as subprime lenders to comprise its population of subprime mortgage loans.

As of December 31, 2007, the Company had not yet applied the loss mitigation approaches as outlined in the ASF Framework. The Company chose to adopt this framework during the first quarter of 2008 and does not expect that its application will impact the off-balance sheet status of the QSPEs that hold these subprime ARM loans.

### Contractual Obligations

The following table presents, as of December 31, 2007, the Company's significant fixed and determinable contractual obligations, within the categories described below, by payment date or contractual maturity. These contractual obligations, except for the operating lease obligations and purchase obligations, are included in the Consolidated Statements of Financial Condition. The most significant purchase obligations are contracts related to services. The payment amounts represent those amounts contractually due to the recipient.

	Payments Due by Period (in millions)				
	Total	Due within One Year	After One but within Three Years	After Three but within Five Years	More than Five Years
<b>Contractual Obligations</b>					
Debt obligations	\$ 106,944	\$ 47,431	\$ 25,645	\$ 18,342	\$ 15,526
Capital lease obligations	47	9	18	8	12
Operating lease obligations	2,074	415	664	410	585
Purchase obligations <sup>(1)</sup>	1,047	279	437	256	75
Total contractual obligations	\$ 110,112	\$ 48,134	\$ 26,764	\$ 19,016	\$ 16,198

NOTE: At December 31, 2007, the liability recorded for uncertain tax positions, excluding associated interest and penalties, was approximately \$500 million pursuant to FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN 48"). This liability represents an estimate of tax positions that the Company has taken in its tax returns which may ultimately not be sustained upon examination by the tax authorities. Since the ultimate amount and timing of any future cash settlements cannot be predicted with reasonable certainty, the estimated FIN 48 liability has been excluded from the contractual obligations table.

(1) Purchase obligations are defined as an agreement to purchase goods or services that is enforceable and legally binding whereby the Company commits to a fixed or minimum purchase amount over a specified period of time. Estimated payments for contracts that may be terminated early without penalty are shown through the first termination date; all others are shown through the date of contract termination. Excluded from the table are purchase obligations expected to be settled in cash within 90 days of the end of the reporting period.

The Company enters into derivative contracts under which the Company is required to either receive cash or pay cash to counterparties depending on changes in interest or foreign exchange rates. Derivative contracts are carried at fair value in the Consolidated Statements of Financial Condition with the fair value representing the net present value of expected future cash receipts or payments based on market interest rates as of the balance sheet date. The fair value of the contracts changes as a result of fluctuations in market interest rates. Further discussion of derivative instruments is included in Notes 1 and 23 to the Consolidated Financial Statements "Summary of Significant Accounting Policies" and "Derivative Financial Instruments."

### **Commitments, Guarantees and Contingencies**

The Company may incur liabilities under certain contractual agreements contingent upon the occurrence of certain events. A discussion of these contractual arrangements under which the Company may be held liable is included in Note 15 to the Consolidated Financial Statements "Commitments, Guarantees and Contingencies." In addition, the Company has commitments and obligations under pension and other postretirement benefit plans as described in Note 22 to the Consolidated Financial Statements "Employee Benefits Programs and Other Expense."

### **Risk Management**

The Company is exposed to four major categories of risk: credit, liquidity, market and operational.

The Company's Chief Enterprise Risk Officer is responsible for enterprise-wide risk management. The Company's Enterprise Risk Management function oversees the identification, measurement, monitoring, control and reporting of credit, market and operational risk. The Company's Treasury function is responsible for the measurement, management and control of liquidity risk. The Internal Audit function, which reports to the Audit Committee of the Board of Directors, independently assesses the Company's compliance with risk management controls, policies and procedures.

The Board of Directors, assisted by the Audit and Finance Committees on certain delegated matters, oversees the monitoring and controlling of significant risk exposures, including the policies governing risk management. The Corporate Relations Committee of the Board of Directors oversees the Company's reputation and those elements of operational risk that impact the Company's reputation. Governance and oversight of credit, liquidity and market risks are provided by the Finance Committee of the Board of Directors. Governance and oversight of operational risk is provided by the Audit Committee of the Board of Directors.

Management's governing risk committee is the Enterprise Risk Management Committee. This committee and its subcommittees include representation from the Company's lines of business and the Enterprise Risk Management function. Subcommittees of the Enterprise Risk Management Committee provide specialized risk governance and include the Credit Risk Management Committee, the Market Risk Committee and the Operational Risk Committee.

Members of the Enterprise Risk Management function work with the lines of business to establish appropriate policies, standards and limits designed to maintain risk exposures within the Company's risk tolerance. Significant risk management policies approved by the relevant management committees are also reviewed and approved by the Audit and Finance Committees. Enterprise Risk Management also provides objective oversight of risk elements inherent in the Company's business activities and practices, oversees compliance with laws and regulations, and reports periodically to the Board of Directors.

Management is responsible for balancing risk and reward in determining and executing business strategies. Business lines, Enterprise Risk Management and Treasury divide the responsibilities of conducting measurement and monitoring of the Company's risk exposures. Risk exceptions, depending

on their type and significance, are elevated to management or Board committees responsible for oversight.

### **Credit Risk Management**

Credit risk is the risk of loss arising from adverse changes in a borrower's or counterparty's actual or perceived ability to meet its financial obligations under agreed-upon terms and exists primarily in lending, securities and derivative portfolios. The degree of credit risk will vary based on many factors including the size of the asset or transaction, the contractual terms of the related documents, the credit characteristics of the borrower, the channel through which assets are acquired, the features of loan products or derivatives, the existence and strength of guarantor support and the availability, quality and adequacy of any underlying collateral. The degree of credit risk and level of credit losses is highly dependent on the economic environment that unfolds subsequent to originating or acquiring assets. The extent of asset diversification and concentrations also affect total credit risk. Credit risk is assessed through analyzing these and other factors.

The Company's credit risk management process provides for management and accountability to be decentralized through our lines of business. The Chief Credit Officer's primary responsibilities include directing the activities of the Credit Risk Management Committee, overseeing portfolio performance and ensuring compliance with established credit policies, standards and limits, determining the reasonableness of the Company's allowance for loan losses, reviewing and approving large credit exposures, and delegating credit approval authorities. Each business segment has a chief risk officer who is primarily responsible for managing credit, market and operational risk within their business segment. Segment chief risk officers have both transaction approval authority and governance authority for the approval of products, programs and guidelines within established policies, standards and limits. The Chief Credit Officer reports directly to the Chief Enterprise Risk Officer. Segment chief risk officers have dual reporting responsibilities to the Chief Enterprise Risk Officer and to their respective segment President.

The Credit Risk Management Committee is comprised of the Chief Credit Officer, business segment chief risk officers, and senior finance, treasury and portfolio management professionals. This Committee addresses a variety of matters including credit strategy and governance and is primarily responsible for approving new or amended credit standards and recommending new or amendments to significant credit policies to the Enterprise Risk Management Committee for approval by the Finance Committee of the Board of Directors.

### **U.S. Housing Market Conditions and their Impact on the Company's Loan Portfolio**

Following a prolonged period of growth, deteriorating conditions in the U.S. housing market that became evident in the first half of 2007 accelerated throughout the remainder of the year. The decline in home price appreciation rates in the first half of 2007 and absolute declines in home prices in the second half of 2007 has been particularly abrupt in California and Florida, where approximately 48% and 10% of the Company's single-family residential mortgage loans at December 31, 2007 are located. The significant and abrupt decline in secondary market liquidity for home loans which are not eligible for sale to housing government-sponsored enterprises ("nonconforming" loans) contributed to the decrease in the availability of housing credit. As many lenders have been forced out of business or have severely curtailed their operations and most remaining lenders have increased nonconforming mortgage interest rates and tightened underwriting standards, many borrowers, particularly subprime borrowers, borrowers in markets with declining housing prices and borrowers wanting nonconforming loans, have been unable either to refinance existing loans or sell their homes. Similarly, certain prospective home buyers have found it both harder to obtain credit and have found credit more expensive. These forces have combined to result in a supply of unsold homes in December 2007 of approximately 9.7 months, a 47% increase from December 2006, which in turn has contributed to a 7% decline in the national



median sales price for existing homes between those same periods. Housing market weakness was also evident in the change in the national volume of foreclosure filings which increased by 75% in 2007 from 2006.

Faced with these unfavorable conditions, an increasing number of borrowers, including those with adjustable-rate mortgages that repriced upward at the expiration of their fixed rate periods, have defaulted on their loans thereby contributing to an increase in delinquency rates. Furthermore, the rate at which delinquent loans moved through delinquency stages towards foreclosure increased in the fourth quarter of 2007. This increase in late stage delinquencies is evident in the ratio of nonperforming assets to total assets which increased from 0.57% at the end of 2005 to 0.80% at the end of 2006 to 2.17% at December 31, 2007. Loss severities on foreclosed assets have also increased more than expected as lower collateral values on foreclosed properties have been insufficient to cover the recorded investment in the loan. Reflecting higher incurred losses inherent in the portfolio resulting primarily from these economic factors, the Company increased its allowance for loan losses, both in absolute terms and as a percentage of loans held in portfolio from \$1.70 billion or 0.74% of loans held in portfolio at the end of 2005 to \$2.57 billion or 1.05% of total loans held in portfolio at December 31, 2007.

#### **Key Factors Affecting Credit Costs: Lien Position, Loan-to-Value Ratios and Loan Vintages**

In a stressed housing market with increasing delinquencies and declining housing prices, such as currently exists, the adequacy of collateral securing a loan becomes an important factor in determining future loan performance as borrowers with more equity in their properties generally have a greater vested interest in keeping their loans current than borrowers with little to no equity in their properties. Generally speaking, homes purchased prior to the end of 2004 have benefited from more home price appreciation than homes purchased more recently. Unless a borrower has withdrawn substantial amounts of equity from the collateralized property, the credit performance of earlier vintage loans in the Company's residential loan portfolio is generally more favorable than loans originated or purchased more recently.

In the event that the Company forecloses on a property, the extent to which the outstanding balance on a loan exceeds its collateral value (less cost to sell) will determine the severity of loss. Generally speaking, properties with higher current loan-to-value ratios would be expected to result in higher severity of loss on foreclosure than properties with lower current loan-to-value ratios. Both loan-to-value ratios at origination and estimated current loan-to-value ratios are key inputs in estimating the allowance for loan losses.

Statistical estimation techniques used to estimate the allowance for loan losses in single family residential portfolios incorporate estimates of changes in housing prices using Office of Federal Housing Enterprise Oversight ("OFHEO") cumulative growth rates available at the time the assessments are conducted. The estimate of the allowance at December 31, 2007 incorporated OFHEO data as of September 30, 2007 as well as more current data evidencing conditions in the housing market, such as provided by the National Associations of Realtors, and internal estimates of future loss severity. On February 26, 2008, OFHEO published its estimate of changes in the housing price index as of December 31, 2007. Estimates of changes in the housing price index made by the Company in the fourth quarter of 2007 were determined to be in-line with those published by OFHEO. As indicated in the footnotes to the loan-to-value/vintage tables that follow, estimated current loan-to-value ratios reflected in the tables are estimated using OFHEO home price index data as of September 30, 2007.

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In foreclosure proceedings, lien position is also a critical determinant of severity of loss because when the Company holds a lien on a property that is subordinate to a first lien mortgage held by another lender, both the probability of loss and severity of loss risk are generally higher than when the Company holds both the first lien home loan and second lien home equity loan or line of credit. In the event of foreclosure, the probability of loss is generally higher because the first lien holder does not have to take into consideration any losses the second lien holder may sustain when deciding whether to foreclose on a property. The severity of loss risk is higher principally because a second lien holder who exercises its right to foreclose on a property must ensure the first lien holder's investment is repaid in full.

The table below analyzes the composition of the unpaid principal balance ("UPB") of home loans held in portfolio at December 31, 2007:

Loan-to-Value Ratio at Origination	Year of Origination				Total UPB	% of Total
	Pre-2005	2005	2006	2007		
(UPB in millions)						
Home loans:						
≤50%	\$ 3,827	\$ 1,278	\$ 845	\$ 2,960	\$ 8,910	8%
>50-60%	4,168	1,826	1,461	4,039	11,494	11
>60-70%	9,445	5,271	3,866	7,867	26,449	24
>70-80%	16,319	11,240	10,277	17,840	55,676	51
>80-90%	1,843	687	608	1,596	4,734	4
>90%	837	184	202	418	1,641	2
Home loans held in portfolio <sup>(1)(2)(3)(4)</sup>	\$ 36,439	\$ 20,486	\$ 17,259	\$ 34,720	\$ 108,904	100%
As a percentage of total UPB	33%	19%	16%	32%	100%	
Average loan-to-value ratio at origination	69	71	72	70	70	
Average estimated current loan-to-value ratio <sup>(5)</sup>	46	66	75	71	62	

(1) Excludes home loans in the subprime mortgage channel.

(2) Excluded from the balances of home loans held in portfolio are \$553 million of home loans that are insured by the Federal Housing Administration ("FHA") or guaranteed by the Department of Veterans Affairs ("VA"), of which \$38 million have loan-to-value ratios of ≤80% and \$515 million have loan-to-value ratios of >80%.

(3) Included in the balance of home loans held in portfolio are the following interest-only home loans and their related loan-to-value ratios at origination: \$28.64 billion (≤80%), \$997 million (>80-90%) and \$253 million (>90%). The volume of interest-only loans amounted to \$18.11 billion in 2007.

(4) The volume of home loans with loan-to-value ratios at origination of >80% amounted to \$8.40 billion in 2007.

(5) The average estimated current loan-to-value ratio reflects the UPB outstanding at the balance sheet date, divided by the estimated current property value. Current property values are estimated using data from the September 30, 2007 Office of Federal Housing Enterprise Oversight ("OFHEO") home price index.

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The table below analyzes the composition of the unpaid principal balance ("UPB") of prime home equity loans and lines of credit held in portfolio at December 31, 2007:

Combined Loan-to-Value Ratio at Origination <sup>(1)</sup>	Year of Origination				Total UPB	% of Total
	Pre-2005	2005	2006	2007		
(UPB in millions)						
Prime home equity loans and lines of credit:						
≤50%	\$ 2,896	\$ 1,340	\$ 1,515	\$ 1,504	\$ 7,255	12%
>50-60%	1,831	931	991	1,038	4,791	8
>60-70%	2,678	1,522	1,550	1,706	7,456	13
>70-80%	6,029	4,233	3,997	4,857	19,116	32
>80-90%	2,730	4,057	5,693	6,624	19,104	32
>90%	618	232	271	567	1,688	3
<hr/>						
Prime home equity loans and lines of credit held in portfolio <sup>(2)(3)(4)(5)</sup>	\$ 16,782	\$ 12,315	\$ 14,017	\$ 16,296	\$ 59,410	100%
<hr/>						
As a percentage of total UPB	28%	21%	24%	27%	100%	
<hr/>						
Average combined loan-to-value ratio at origination <sup>(1)</sup>	68	74	75	76	73	
Average estimated current combined loan-to-value ratio <sup>(1)(6)</sup>	49	65	73	76	65	

- (1) The combined loan-to-value ratio at origination measures the ratio of the original loan amount of the first lien product (typically a first lien mortgage loan) and the original loan amount of the second lien product (typically a second lien home equity loan or line of credit) to the appraised value of the underlying collateral at origination. Where the second lien product is a line of credit, the total commitment amount is used in calculating the combined loan-to-value ratio.
- (2) Excludes home equity loans in the subprime mortgage channel.
- (3) 27% of prime home equity loans and lines of credit were in first lien position at December 31, 2007.
- (4) The Company has pool mortgage insurance that generally insulates it from the risk of default on certain prime home equity loans and lines of credit originated after March 2004 where the combined loan-to-value ratio at origination is greater than 90 percent. Contractual stop loss provisions limit the insurer's exposure to 10% of the outstanding loan balance for loans originated prior to December 31, 2006, and 8% for loans originated thereafter.
- (5) The volume of prime home equity loans and lines of credit with combined loan-to-value ratios at origination of >80% amounted to \$10.10 billion in 2007.
- (6) The average estimated current combined loan-to-value ratio reflects the UPB outstanding or commitment amount (in the case of lines of credit) at the balance sheet date, divided by the estimated current property value. Current property values are estimated using data from the September 30, 2007 OFHEO home price index.

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The unpaid principal balance ("UPB") of prime home equity loans and lines of credit held in portfolio at December 31, 2007, as shown in the immediately preceding table, included the following home equity loans and lines of credit in *junior lien* position:

Combined Loan-to-Value Ratio at Origination <sup>(1)</sup>	Year of Origination				Total UPB	% of Total
	Pre-2005	2005	2006	2007		
(UPB in millions)						
Prime <i>junior lien</i> home equity loans and lines of credit:						
≤50%	\$ 1,015	\$ 654	\$ 922	\$ 729	\$ 3,320	8%
>50-60%	905	642	832	685	3,064	7
>60-70%	1,533	1,158	1,365	1,148	5,204	12
>70-80%	3,798	3,381	3,573	3,349	14,101	32
>80-90%	2,303	3,694	5,461	5,181	16,639	38
>90%	338	100	212	496	1,146	3
Total prime <i>junior lien</i> home equity loans and lines of credit held in portfolio <sup>(2)(3)</sup>	\$ 9,892	\$ 9,629	\$ 12,365	\$ 11,588	\$ 43,474	100%
As a percentage of total UPB	23%	22%	28%	27%	100%	
Average combined loan-to-value ratio at origination <sup>(1)</sup>	73	76	77	78	76	
Average estimated current combined loan-to-value ratio <sup>(1)(4)</sup>	54	68	75	78	69	

(1) The combined loan-to-value ratio measures the ratio of the original loan amount of the first lien product (typically a first lien mortgage loan) and the original loan amount of the second lien product (typically a second lien home equity loan or line of credit) to the appraised value of the underlying collateral. Where the second lien product is a line of credit, the total commitment amount is used in calculating the combined loan-to-value ratio.

(2) Excludes home equity loans in the subprime mortgage channel.

(3) The Company has pool mortgage insurance that generally insulates it from the risk of default on certain prime home equity loans and lines of credit originated after March 2004 where the combined loan-to-value ratio at origination is greater than 90 percent. Contractual stop loss provisions limit the insurer's exposure to 10% of the outstanding loan balance for loans originated prior to December 31, 2006, and 8% for loans originated thereafter.

(4) The average estimated current combined loan-to-value ratio reflects the UPB outstanding or commitment amount (in the case of lines of credit) at the balance sheet date, divided by the estimated current property value. Current property values are estimated using data from the September 30, 2007 OFHEO home price index.

### *Option ARM Home Loans*

The Option ARM home loan product is an adjustable-rate mortgage loan that provides the borrower with the option each month to make a fully-amortizing, interest-only, or minimum payment. As described in greater detail below, the minimum payment is typically insufficient to cover interest accrued in the prior month and any unpaid interest is deferred and added to the principal balance of the loan. In the current housing market, the popularity of Option ARM loans has decreased and loan volumes have declined from \$65.16 billion in 2005 to \$42.59 billion in 2006 to \$25.78 billion in 2007.

### Loan Features

The minimum payment on an Option ARM loan is based on the interest rate charged during the introductory period. This introductory rate has usually been significantly below the fully-indexed rate. The fully-indexed rate is calculated using an index rate plus a margin. Once the introductory period ends, the contractual interest rate charged on the loan increases to the fully-indexed rate and adjusts monthly to reflect

movements in the index.

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If the borrower continues to make the minimum monthly payment after the introductory period ends, the payment may not be sufficient to cover interest accrued in the previous month. In this case, the loan will "negatively amortize" as unpaid interest is deferred and added to the principal balance of the loan. The minimum payment on an Option ARM loan is adjusted on each anniversary date of the loan but each increase or decrease is limited to a maximum of 7.5% of the minimum payment amount on such date until a "recasting event" occurs.

A recasting event occurs every 60 months or sooner upon reaching a negative amortization cap. When a recasting event occurs, a new minimum monthly payment is calculated without regard to any limits on the increase or decrease in amount that would otherwise apply under the annual 7.5% payment cap. This new minimum monthly payment is calculated to be sufficient to fully repay the principal balance of the loan, including any theretofore deferred interest, over the remainder of the loan term using the fully-indexed rate then in effect. A recasting event occurs immediately whenever the unpaid principal balance reaches the negative amortization cap, which is expressed as a percent of the original loan balance. Prior to 2006, the negative amortization cap was 125% of the original loan balance (or 110% of the original loan balance for loans secured by property located in New York and loans purchased through the correspondent channel). For all Option ARM loans originated in 2006, the negative amortization cap was 110% of the original loan balance. For Option ARM loans originated in 2007, the negative amortization cap was raised to 115%, with the exception of loans secured by property located in New York and loans purchased through the correspondent channel where the negative amortization cap remains at 110%. Declines in mortgage rates to which Option ARM loans are indexed will generally delay the timeframe within which negatively amortizing Option ARM loans reach their negative amortization caps. Conversely, increases in mortgage rates to which Option ARM loans are indexed will generally accelerate the timeframe within which negatively amortizing Option ARM loans reach their negative amortization caps.

In the first month that follows a recasting event, the minimum payment will equal the fully-amortizing payment. If in subsequent months the index rate decreases, the minimum payment may exceed the fully-amortizing payment. Conversely, if the index rate increases in subsequent months, negative amortization may resume. In this situation, the 7.5% annual payment cap will once again operate to limit the change in the minimum payment until another recasting event occurs.

Assuming all Option ARM loans recast no earlier than five years after origination, as of December 31, 2007, 8% of the Company's Option ARM portfolio is scheduled to recast in 2008 and 13% is scheduled to recast in 2009.

Loan Performance

The table below analyzes the composition of the unpaid principal balance ("UPB") of Option ARM home loans held in portfolio at December 31, 2007:

Loan-to-Value Ratio at Origination	Year of Origination				Total UPB	% of Total
	Pre-2005	2005	2006	2007		
(UPB in millions)						
Home loan Option ARMs						
≤50%	\$ 1,202	\$ 719	\$ 458	\$ 753	\$ 3,132	5%
>50-60%	1,439	1,076	883	1,344	4,742	8
>60-70%	4,327	3,525	2,835	3,333	14,020	24
>70-80%	8,521	7,429	8,421	8,519	32,890	57
>80-90%	1,017	495	504	939	2,955	5
>90%	288	92	152	125	657	1
Total home loan Option ARMs held in portfolio	\$ 16,794	\$ 13,336	\$ 13,253	\$ 15,013	\$ 58,396	100%
As a percentage of total UPB	29%	23%	23%	25%	100%	
Average loan-to-value ratio at origination	71	71	73	73	72	
Average estimated current loan-to-value ratio <sup>(1)</sup>	48	69	77	74	66	

(1) The average estimated current loan-to-value ratio reflects the UPB outstanding at the balance sheet date, divided by the estimated current property value. Current property values are estimated using data from the September 30, 2007 OFHEO home price index.

Key statistics for Option ARM loans held in the Company's home loan portfolio are set forth in the following table:

	December 31,		
	2007	2006	2005
(dollars in millions)			
Loan balance	\$ 58,870	\$ 63,557	\$ 71,201
Capitalized interest recognized in earnings that resulted from negative amortization	1,418	1,068	292
Total amount by which the unpaid principal balance exceeded the original principal amount	1,731	888	160
Balance of loans that experienced a net increase in negative amortization during the year	48,162	48,832	44,796
Percentage of borrowers whose final loan payment of the year resulted in negative amortization:			
By number of loans	50%	51%	42%
By value of loans	69	68	56

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The table below provides geographic distribution of the Company's home loan Option ARM portfolio at December 31, 2007:

	Portfolio	Weighted Average Estimated Current Loan-to-Value Ratio
(dollars in millions)		
California	\$ 28,956	49%
Florida	7,605	13
New York/New Jersey	5,333	9
Washington/Oregon	2,186	3
Illinois	1,506	3
Texas	528	1
Other	12,756	22
Total home loan Option ARMs held in portfolio	\$ 58,870	100%

### *Subprime Mortgage Channel*

In the fourth quarter of 2007, the Company discontinued all lending in its subprime mortgage channel. This channel is comprised of loans originated under the Company's Long Beach Mortgage name or were purchased from lenders who were generally recognized as lending to subprime borrowers ("Subprime Lenders"). The Company did not originate or purchase loan products with negative amortization features through its subprime mortgage channel. The Company separately reports the performance of loans in its subprime mortgage channel as such loans generally experience higher delinquencies and net charge-offs than prime mortgage loans that possess comparable loan-to-value ratios and credit scores. To compensate for the increased credit risk of such loans, the Company generally charged such borrowers a higher rate of interest than borrowers in the prime channel. As of December 31, 2007, subprime mortgage channel loans held for investment totaled \$18.62 billion, including \$2.53 billion of home equity loans.

Subprime mortgage channel loans are managed by a dedicated collections department with collectors experienced in subprime mortgage loan collections. Servicing activities for these loans emphasize direct contact with customers at early stages of delinquency based on a customer's risk profile, and the Company uses automated telephone dialing and call distribution systems to increase the effectiveness of collection calls. Customized payment plans and work-out plans may be used to return delinquent loans to current status. When delinquent loans become 120 days contractually past due, the loan foreclosure process typically begins. Loans are restructured on a selective basis, so as to minimize loss during the collections and foreclosure process.



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The unpaid principal balances ("UPB") of subprime mortgage channel loans held in portfolio at December 31, 2007 was as follows:

Loan-to-Value Ratio at Origination	Year of Origination					Total UPB	% of Total
	Pre-2005	2005	2006	2007	Total UPB		
(UPB in millions)							
<b>Subprime mortgage channel:</b>							
≤50%	\$ 213	\$ 111	\$ 252	\$ 61	\$ 637	3%	
>50-60%	259	150	229	87	725	4	
>60-70%	533	341	504	209	1,587	9	
>70-80%	1,704	2,527	2,382	838	7,451	40	
>80-90%	1,827	1,246	2,054	660	5,787	31	
>90%	34	134	1,912	247	2,327	13	
 Total subprime mortgage channel loans held in portfolio	 \$ 4,570	 \$ 4,509	 \$ 7,333	 \$ 2,102	 \$ 18,514	 100%	
 As a percentage of total UPB	 25%	 24%	 40%	 11%	 100%		
Average loan-to-value ratio at origination <sup>(1)</sup>	77	79	83	80	80		
Average estimated current loan-to-value ratio <sup>(2)</sup>	57	71	82	81	73		

(1) Origination loan-to-value used for first liens and combined loan-to-value used for second liens.

(2) The estimated current loan-to-value ratio reflects the UPB outstanding at the balance sheet date, divided by the estimated current property value. Current property values are estimated using data from the September 30, 2007 OFHEO home price index.

### Nonaccrual Loans, Foreclosed Assets and Restructured Loans

Loans, excluding credit card loans, are generally placed on nonaccrual status upon reaching 90 days past due. Additionally, individual loans in non-homogeneous portfolios are placed on nonaccrual status prior to becoming 90 days past due when payment in full of principal or interest by the borrower is not expected. Restructured loans are reported as nonaccrual loans and interest received on such loans is accounted for using the cash method until such time as the Company determines that collectibility of principal and interest is reasonably assured, at which point the loan is returned to accrual status and reported as an accruing restructured loan. At December 31, 2007, restructured loans of \$633 million were reported as nonaccrual loans in accordance with the Company's policy, accounting for 19 basis points of the 217 basis points of the nonperforming assets to total assets ratio.

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Nonaccrual loans and foreclosed assets ("nonperforming assets") consisted of the following:

	December 31,				
	2007	2006	2005	2004	2003
	(dollars in millions)				
<b>Nonperforming assets:</b>					
Nonaccrual loans <sup>(1)(2)(3)</sup> :					
Loans secured by real estate:					
Home loans <sup>(4)</sup>	\$ 2,302	\$ 640	\$ 565	\$ 534	\$ 736
Home equity loans and lines of credit <sup>(4)</sup>	835	231	87	66	47
Subprime mortgage channel <sup>(5)</sup>	2,721	1,283	873	682	597
Home construction <sup>(6)</sup>	56	27	10	28	35
Multi-family	131	46	25	12	19
Other real estate	53	51	70	162	153
	<b>6,098</b>	<b>2,278</b>	<b>1,630</b>	<b>1,484</b>	<b>1,587</b>
Total nonaccrual loans secured by real estate					
Consumer	1	1	8	9	8
Commercial	24	16	48	41	31
	<b>6,123</b>	<b>2,295</b>	<b>1,686</b>	<b>1,534</b>	<b>1,626</b>
Total nonaccrual loans held in portfolio					
Foreclosed assets <sup>(7)</sup>	979	480	276	261	311
	<b>7,102</b>	<b>2,775</b>	<b>1,962</b>	<b>1,795</b>	<b>1,937</b>
Total nonperforming assets <sup>(8)</sup>					
	<b>\$ 7,102</b>	<b>\$ 2,775</b>	<b>\$ 1,962</b>	<b>\$ 1,795</b>	<b>\$ 1,937</b>
	<b>2.17%</b>	<b>0.80%</b>	<b>0.57%</b>	<b>0.58%</b>	<b>0.70%</b>
Total nonperforming assets as a percentage of total assets					

- (1) If interest on nonaccrual loans under the original terms had been recognized, such income is estimated to have been \$246 million in 2007, \$118 million in 2006, \$79 million in 2005, \$64 million in 2004 and \$86 million in 2003.
- (2) Nonaccrual loans held for sale, which are excluded from the nonaccrual balances presented above, were \$4 million, \$185 million, \$245 million, \$76 million and \$66 million at December 31, 2007, 2006, 2005, 2004 and 2003. Loans held for sale are accounted for at the lower of cost or fair value, with valuation changes included as adjustments to noninterest income.
- (3) Credit card loans are exempt under regulatory rules from being classified as nonaccrual because they are charged off when they are determined to be uncollectible, or by the end of the month in which the account becomes 180 days past due.
- (4) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (5) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (6) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.
- (7) Foreclosed real estate securing Government National Mortgage Association ("GNMA") loans of \$37 million, \$99 million, \$79 million, \$79 million and \$82 million at December 31, 2007, 2006, 2005, 2004 and 2003 have been excluded. These assets are fully collectible as the corresponding GNMA loans are insured by the Federal Housing Administration ("FHA") or guaranteed by the Department of Veterans Affairs ("VA").
- (8) Excludes accruing restructured loans of \$251 million, \$314 million, \$296 million, \$293 million and \$249 million at December 31, 2007, 2006, 2005, 2004 and 2003.

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Loans held in portfolio (excluding the allowance for loan losses) and the nonaccrual component thereof, in each instance excluding credit card loans, by geographic concentration at December 31, 2007 were as follows:

	California		New York/New Jersey		Florida	
	Portfolio	Nonaccrual	Portfolio	Nonaccrual	Portfolio	Nonaccrual
(dollars in millions)						
Loans secured by real estate:						
Home loans <sup>(1)</sup>	\$ 53,299	\$ 762	\$ 11,528	\$ 253	\$ 11,027	\$ 464
Home equity loans and lines of credit <sup>(1)</sup>	32,499	489	4,957	53	5,469	115
Subprime mortgage channel <sup>(2)</sup>	4,742	807	2,053	285	1,815	302
Home construction <sup>(3)</sup>	1,251	34	79	4	121	7
Multi-family	20,335	14	5,405	57	747	21
Other real estate	5,056	16	1,769	4	171	1
Total loans secured by real estate	117,182	2,122	25,791	656	19,350	910
Consumer	87	1	18		13	
Commercial	514	6	229	4	200	3
Total loans and nonaccrual loans held in portfolio	\$ 117,783	\$ 2,129	\$ 26,038	\$ 660	\$ 19,563	\$ 913

Loans and nonaccrual loans as a percentage of total loans and total nonaccrual loans	50%	35%	11%	11%	8%	15%
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- (1) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (2) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (3) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.

	Washington/Oregon		Texas		Illinois	
	Portfolio	Nonaccrual	Portfolio	Nonaccrual	Portfolio	Nonaccrual
(dollars in millions)						
Loans secured by real estate:						
Home loans <sup>(1)</sup>	\$ 5,324	\$ 50	\$ 1,306	\$ 30	\$ 3,497	\$ 95
Home equity loans and lines of credit <sup>(1)</sup>	6,359	31	3,271	15	1,338	21
Subprime mortgage channel <sup>(2)</sup>	718	61	1,130	116	869	147
Home construction <sup>(3)</sup>	320	4	26		36	
Multi-family	1,588		483	11	744	7
Other real estate	697	2	673	19	50	
Total loans secured by real estate	15,006	148	6,889	191	6,534	270
Consumer	54		14		1	

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	Washington/Oregon		Texas		Illinois	
Commercial	123	1	223	3	64	1
Total loans and nonaccrual loans held in portfolio	\$ 15,183	\$ 149	\$ 7,126	\$ 194	\$ 6,599	\$ 271
Loans and nonaccrual loans as a percentage of total loans and total nonaccrual loans	7%	2%	3%	3%	3%	4%

- (1) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (2) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (3) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.

	Other <sup>(4)</sup>		Total	
	Portfolio	Nonaccrual	Portfolio	Nonaccrual
(dollars in millions)				
<b>Loans secured by real estate:</b>				
Home loans <sup>(1)</sup>	\$ 24,406	\$ 648	\$ 110,387	\$ 2,302
Home equity loans and lines of credit <sup>(1)</sup>	7,070	111	60,963	835
Subprime mortgage channel <sup>(2)</sup>	7,290	1,003	18,617	2,721
Home construction <sup>(3)</sup>	393	7	2,226	56
Multi-family	2,452	21	31,754	131
Other real estate	1,108	11	9,524	53
<b>Total loans secured by real estate</b>	<b>42,719</b>	<b>1,801</b>	<b>233,471</b>	<b>6,098</b>
Consumer	18		205	1
Commercial	526	6	1,879	24
<b>Total loans and nonaccrual loans held in portfolio</b>	<b>\$ 43,263</b>	<b>\$ 1,807</b>	<b>\$ 235,555<sup>(5)</sup></b>	<b>\$ 6,123</b>

Loans and nonaccrual loans as a percentage of total loans and total nonaccrual loans	18%	30%	100%	100%
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- (1) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (2) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (3) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.
- (4) Of this category, Colorado had the largest portfolio balance of approximately \$4.03 billion and Massachusetts had the largest nonaccrual balance of \$183 million.
- (5) Excludes credit card loans of \$8.83 billion.

The Company monitors delinquency rates for all loans held in portfolio. Increasing early stage delinquency rates (i.e., loans 30-89 days past due) are indicative of possible future credit problems when the Company has serious doubts as to the ability of such borrowers to cure the delinquency condition. Such loans have exhibited a greater propensity to migrate into nonaccrual status as cure rates on early-stage delinquencies deteriorated during the latter part of 2007. The delinquency rate for home loans and home equity loans and lines of credit that were more than 30 days past due but less than 90 days past due amounted to 1.43% and 2.02% at December 31, 2007 as compared to 0.68% and 0.89% at December 31, 2006.

### Credit Card Loans

The Company offers a wide selection of credit cards to consumers and small businesses. Products offered include Washington Mutual-branded credit cards, as well as a variety of affinity and co-branded credit cards.

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Credit cards provide borrowers with revolving, generally unsecured lines of credit that are used to make purchases and obtain cash advances primarily through Visa and MasterCard credit card networks. Credit card loans typically have smaller balances, shorter lifecycles and experience higher delinquency and loss rates than secured real estate loans. To offset the higher risk of loss inherent in unsecured credit card loans, interest rates and fees are generally structured to generate higher yields than secured real estate loans.

The Company selectively targets customers that are often underserved by large prime/superprime-oriented credit card issuers and who satisfy its underwriting criteria. The Company uses an automated underwriting process that includes an assessment of an applicant's credit profile and expected payment performance when reviewing credit card applications. The Company has been successful in selling credit cards to its existing retail customers.

Account management efforts, seasoning, and economic conditions all affect overall credit quality. The Company monitors customers' risk profiles regularly to optimize loss exposure over time and reserves the right under its credit card account agreement to change or terminate at any time, subject to applicable notice requirements, any terms, conditions, services, or features of the agreement. In cases where the customer fails to comply with the account agreement or presents a higher credit risk, the Company may restrict further use of the card, close the account, increase the interest rate, and/or pursue collection efforts.

Collection efforts are performed on accounts that are delinquent and for accounts that are current but over their credit limit. The Company uses a delinquency lifecycle strategy, in combination with behavior-driven approaches, consumer counseling, and consumer debt management programs, to manage delinquent accounts. Under the delinquency lifecycle strategy, the Company prioritizes collections to focus on delinquency status, with attention to customer events within each stage of delinquency.

### **Allowance for Loan Losses**

The allowance for loan losses represents management's estimate of incurred credit losses inherent in the Company's loan portfolio as of the balance sheet date. The estimate of the allowance is based on a variety of factors, including past loan loss experience, the current credit profile of borrowers, adverse situations that have occurred that may affect a borrower's ability to meet his financial obligations, the estimated value of underlying collateral, general economic conditions, and the impact that changes in interest rates and unemployment levels have on a borrower's ability to repay adjustable-rate loans. Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. The Company maintains a comprehensive governance structure and a certification and validation process that is designed to support, among other things, the appropriateness of the estimate of the allowance for loan losses. Subsequent evaluations of the loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for loan losses in future periods.

The Company separately evaluates the impairment of the homogeneous and non-homogeneous loan portfolios. The homogeneous portfolio, comprising substantially all loans held in portfolio, is evaluated for collective impairment and consists predominantly of home loans, home equity loans and lines of credit, credit card loans and most commercial business, commercial real estate and multi-family loans. Certain home mortgage loans whose terms have been modified through debt restructurings and non-homogeneous loans are evaluated for individual impairment. In 2005, the Company defined non-homogeneous loans as commercial business, commercial real estate and multi-family loans with a current balance in excess of \$1 million or loans with a current balance less than \$1 million and highly risk rated. Beginning in 2006, reflecting (a) a shift in business practice towards originating and retaining in portfolio, multi-family loans whose performance could be modeled using a formulaic, statistical-based approach, and (b) the introduction of a new multi-family loan loss model that incorporated default-predictive variables that enabled the Company to make a more robust estimate of incurred losses on loans in this portfolio, the Company redefined non-homogeneous loans as certain commercial business, commercial real estate and multi-family loans with an unpaid principal balance in excess of \$3 million.

The Company accounts for the allowance for loan losses on its portfolio of homogeneous loans in accordance with FASB Statement No. 5, *Accounting for Contingencies* ("Statement No. 5"), recording an

allowance when (a) available information indicates that it is probable that a loss has been incurred and (b) the amount of the loss can be reasonably estimated. Generally, borrowers are impacted by events that result in loan default and eventual loss well in advance of the Company's knowledge of those events. Examples of such loss-causing events for home loans are borrower job loss, divorce and medical crisis. An example for commercial real estate loans would be the loss of a major tenant.

The Company allocates a portion of the allowance to the homogeneous loan portfolios and estimates this allocated portion based on analyses of pools of loans with similar credit risk attributes. The Company also estimates an unallocated portion of the allowance that reflects management's assessment of various risk factors that are not fully captured by the statistical estimation techniques used to determine the allocated component of the allowance. However, both the allocated component and the portion that remains unallocated are available to absorb credit losses inherent in the homogeneous loan portfolio as of the balance sheet date.

Statistical estimation techniques are used to determine the allocated allowance for homogeneous loans. Formulaic assessments of credit risk are primarily performed using the Loan Performance Risk Model. Statistical estimation techniques assess default and loss outcomes based on an evaluation of past performance of similar pools of loans in our portfolio, and other factors affecting default and loss factors, as well as industry historical loan loss data. Loss estimation techniques used in statistical models are supplemented by qualitative information to assist in estimating the allocated allowance. When housing prices are volatile, lags in data collection and reporting increase the likelihood of adjustments being made to the allowance. More current data evidencing conditions in the housing market are obtained from analyzing data from the National Association of Realtors on median sales and on housing inventory levels.

Management routinely and regularly evaluates the accuracy of its statistical models and analyzes the performance of loans held in portfolio and makes improvements to those models as facts and circumstances warrant. In addition, the Company refines its estimates and assumptions used to calibrate particular models in response to new data and dynamic market conditions. As necessary and for the same reasons, the Company updates the relative weightings assigned to classes of inputs or factors considered in its particular models. The Company also considers whether the statistical models fully capture estimates of losses related to loans held in portfolio and to the extent adjustments are needed, they are incorporated into the allowance for loan losses.

The Loan Performance Risk Model produces an estimate of the cumulative loss over the remaining terms of the loans by analyzing loan-level data, the key attributes of which are static collateral variables including property type, loan type, lien type, original balance, original loan-to-value ratio and documentation type; ARM-specific variables, such as ARM caps, floors and resets; dynamic variables, such as estimated current loan-to-value ratios and the age of the loan; borrower variables, such as original credit score and delinquency history; and market conditions, such as housing price appreciation or depreciation rates by metropolitan statistical area, and interest rates. Management then estimates the incurred portion of the cumulative loss when estimating its allowance for loan losses.

The unallocated component of the allowance reflects management's evaluation of conditions that are not fully captured in determining the allocated allowance for homogenous loans. The weighting system used in estimating the appropriateness of the unallocated allowance reflects the relative significance of the following factors that are routinely and regularly reviewed: national and local economic trends and conditions (such as gross domestic product and unemployment trends); market conditions (such as changes in housing prices); industry and borrower concentrations within portfolio segments (including concentrations by metropolitan statistical area); recent loan portfolio performance (such as changes in the levels and trends in delinquencies and impaired loans); trends in loan growth (including the velocity of change in loan growth); changes in underwriting criteria; and the regulatory and public policy environment.



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In determining the allowance for loans evaluated for individual impairment and deemed to be impaired, the Company applies the provisions of FASB Statement No. 114, *Accounting by Creditors for Impairment of a Loan* ("Statement No. 114"). Impairment of restructured home loans is measured by aggregating loans with common risk characteristics and calculating the present value of expected future cash flows using historical statistics such as average recovery period and average recovery amount, along with a composite effective interest rate. Impairment on non-homogeneous loans is measured principally using the fair value of the underlying collateral, since such loans are generally collateral dependent. In estimating the fair value of collateral, the Company evaluates various factors, such as occupancy and rental rates in the relevant real estate markets and their effect on the value of the collateral.

When available information confirms that specific loans or portions thereof are uncollectible, those amounts are charged off against the allowance for loan losses. The existence of some or all of the following conditions will generally confirm that a loss has been incurred: the loan is significantly delinquent and the borrower has not demonstrated the ability to bring the loan current; the borrower has insufficient assets to repay the debt; or the fair value of the loan collateral is significantly below the current loan balance and there is little or no prospect for improvement. When home loans and home equity loans and lines of credit become 180 days past due, the portion of the loan balance in excess of the fair value of the underlying collateral (less estimated cost to sell) is charged off against the allowance for loan losses. Credit card loans are charged-off when they are determined to be uncollectible or by the end of the month in which the account becomes 180 days past due.

Like all depository institutions with federal thrift charters, our subsidiary depository institutions continue to be subject to examination by their primary regulator, the OTS. The OTS examinations occur throughout the year and target various activities of our subsidiary depository institutions.

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Changes in the allowance for loan losses were as follows:

	Year Ended December 31,				
	2007	2006	2005	2004	2003
	(dollars in millions)				
Balance, beginning of year	\$ 1,630	\$ 1,695	\$ 1,301	\$ 1,250	\$ 1,503
Allowance transferred to loans held for sale	(550)	(401)	(270)	(23)	(3)
Allowance acquired through business combinations		30	592		
Other	7				17
Provision for loan losses <sup>(1)</sup>	3,107	816	316	209	42
	<u>4,194</u>	<u>2,140</u>	<u>1,939</u>	<u>1,436</u>	<u>1,559</u>
Loans charged off:					
Loans secured by real estate:					
Home loans <sup>(2)</sup>	(214)	(50)	(38)	(39)	(65)
Home equity loans and lines of credit <sup>(2)</sup>	(437)	(31)	(30)	(22)	(14)
Subprime mortgage channel <sup>(3)</sup>	(566)	(140)	(50)	(39)	(39)
Home construction <sup>(4)</sup>		(8)	(1)	(1)	(2)
Multi-family	(5)		(1)	(2)	(5)
Other real estate	(2)	(5)	(8)	(11)	(97)
Total loans secured by real estate	<u>(1,224)</u>	<u>(234)</u>	<u>(128)</u>	<u>(114)</u>	<u>(222)</u>
Consumer:					
Credit card	(448)	(322)	(138)		
Other	(8)	(19)	(38)	(53)	(69)
Commercial	(76)	(28)	(34)	(21)	(79)
Total loans charged off	<u>(1,756)</u>	<u>(603)</u>	<u>(338)</u>	<u>(188)</u>	<u>(370)</u>
Recoveries of loans previously charged off:					
Loans secured by real estate:					
Home loans <sup>(2)</sup>	6	1			10
Home equity loans and lines of credit <sup>(2)</sup>	13	8	9	4	1
Subprime mortgage channel <sup>(3)</sup>	16	6	3	3	3
Home construction <sup>(4)</sup>	1				
Multi-family		1	3	3	1
Other real estate	5	2	13	10	17
Total loans secured by real estate	<u>41</u>	<u>18</u>	<u>28</u>	<u>20</u>	<u>32</u>
Consumer:					
Credit card	75	53	40		
Other	7	14	19	19	15
Commercial	10	8	7	14	14
Total recoveries of loans previously charged off	<u>133</u>	<u>93</u>	<u>94</u>	<u>53</u>	<u>61</u>
Net charge-offs	<u>(1,623)</u>	<u>(510)</u>	<u>(244)</u>	<u>(135)</u>	<u>(309)</u>
Balance, end of year	<u>\$ 2,571</u>	<u>\$ 1,630</u>	<u>\$ 1,695</u>	<u>\$ 1,301</u>	<u>\$ 1,250</u>
Net charge-offs as a percentage of average loans held in portfolio	0.72%	0.21%	0.11%	0.07%	0.20%
Allowance as a percentage of loans held in portfolio	1.05	0.72	0.74	0.63	0.71

(1) Includes a \$202 million reversal of provision for loan losses recorded in the fourth quarter of 2003.

(2)

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- (3) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (3) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (4) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.

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The allowance for loan losses increased slightly from \$1.25 billion at December 31, 2003 to \$1.30 billion at December 31, 2004 reflecting the growth in the loan portfolio. However, the allowance for loan losses as a percentage of loans held in portfolio declined from 0.71% at December 31, 2003 to 0.63% at December 31, 2004 reflecting the continuing strength of the U.S. housing market facilitated by a relatively benign credit environment throughout the year. The favorable credit climate, as well as the sales and runoff of higher risk portfolios in 2003, resulted in much lower net charge-offs in 2004.

The allowance for loan losses increased \$394 million from \$1.30 billion at December 31, 2004 to \$1.70 billion at December 31, 2005 largely reflecting the addition of the credit card portfolio of the former Provident Financial Corporation on October 1, 2005. Largely as a result of this addition, the allowance for loan losses expressed as a percentage of total loans held in portfolio increased from 0.63% at December 31, 2004 to 0.74% at December 31, 2005. Despite increases in short-term interest rates, the overall credit environment during 2005 was relatively stable, fostered by strong employment and real estate markets.

The allowance for loan losses decreased \$65 million from \$1.70 billion at December 31, 2005 to \$1.63 billion at December 31, 2006. The allowance for loans losses as a percentage of total loans held in portfolio, declined from 0.74% at December 31, 2005 to 0.72% at December 31, 2006, due to several factors. The credit profile of the Company's credit card portfolio improved due to the sale of higher risk credit card accounts and from a lower level of bankruptcy-related charge-offs. Delinquency rates on owned credit card loans declined from 3.08% at December 31, 2005 to 2.66% at December 31, 2006. Credit card delinquency rates are one of the key drivers of credit losses in the credit card portfolio and the Company correspondingly reduced the allowance related to credit card receivables. Additionally, the allowance for loan losses was reduced as a result of two primary changes in the assumptions and methodologies used to estimate the allowance attributable to multi-family loans. First, as part of its ongoing program of model improvement, the Company introduced a new model to estimate incurred losses on multi-family loans in 2006. The new model uses a formulaic statistical-based approach for determining loss factors based on relevant default-predictive variables such as loan-to-value and debt service coverage ratios, and geographic factors. The model that was replaced used the same underlying classes of inputs but categorized loans for collective review using the risk grade assigned to them for bank regulatory purposes, the categorization of which inherently involved management judgment. The Company expects this new methodology to result in a better estimate of incurred loss, with greater consistency across periods; it is also more consistent with risk assessment practices in the commercial lending industry. The Company also adopted three year loss confirmation periods for multi-family loans and loans originated or purchased through the subprime mortgage channel, in each case replacing the four year estimate of the loss confirmation period.

The allowance for loan losses increased \$941 million from \$1.63 billion at December 31, 2006 to \$2.57 billion at December 31, 2007 reflecting higher incurred losses inherent in the home loans portfolio, home equity loans and lines of credit portfolio, and in the subprime mortgage channel portfolio resulting primarily from deteriorating conditions in the U.S housing market during 2007. Accordingly the allowance for loan losses as a percentage of total loans held in portfolio increased from 0.72% at December 31, 2006 to 1.05% at December 31, 2007. Adverse trends in key housing market indicators, including growing inventories of unsold homes, rising foreclosure rates and a significant contraction in the availability of credit for nonconforming mortgage products were significant factors that resulted in the increase in the allowance. As a result of these factors, the Company increased its allowance for loan losses with the expectation that it would experience significantly higher credit costs throughout its single-family residential mortgage portfolio.

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An analysis of the allowance for loan losses was as follows:

December 31,

	2007			2006			2005		
	Allowance for Loan Losses	Allocated Allowance of Loan Category	Loan Category as a % of Total Loans <sup>(1)</sup>	Allowance for Loan Losses	Allocated Allowance as a % of Loan Category	Loan Category as a % of Total Loans <sup>(1)</sup>	Allowance for Loan Losses	Allocated Allowance as a % of Loan Category	Loan Category as a % of Total Loans <sup>(1)</sup>
(dollars in millions)									
Allocated allowance:									
Loans secured by real estate:									
Home loans <sup>(2)</sup>	\$ 322	0.29%	45.17%	\$ 202	0.20%	44.22%	\$ 222	0.19%	49.71%
Home equity loans and lines of credit <sup>(2)</sup>	568	0.93	24.95	184	0.35	23.51	106	0.21	22.14
Subprime mortgage channel <sup>(3)</sup>	643	3.45	7.62	326	1.57	9.23	374	1.77	9.21
Home construction <sup>(4)</sup>	7	0.32	0.91	5	0.24	0.93	6	0.29	0.89
Multi-family	105	0.33	12.99	85	0.28	13.41	122	0.48	11.15
Other real estate	63	0.67	3.90	54	0.80	2.99	69	1.37	2.19
<b>Total allocated allowance secured by real estate</b>	<b>1,708</b>	<b>0.73</b>	<b>95.54</b>	<b>856</b>	<b>0.40</b>	<b>94.29</b>	<b>899</b>	<b>0.41</b>	<b>95.29</b>
Consumer:									
Credit card	504	5.71	3.61	508	4.68	4.83	328	4.08	3.50
Other	6	2.90	0.08	7	2.32	0.12	27	4.25	0.28
Commercial	85	4.54	0.77	45	2.64	0.76	44	2.03	0.93
<b>Total allocated allowance held in portfolio</b>	<b>2,303</b>	<b>0.94</b>	<b>100.00</b>	<b>1,416</b>	<b>0.63</b>	<b>100.00</b>	<b>1,298</b>	<b>0.57</b>	<b>100.00</b>
Unallocated allowance	268	0.11		214	0.09		397	0.17	
<b>Total allowance for loan losses</b>	<b>\$ 2,571</b>	<b>1.05%</b>	<b>100.00%</b>	<b>\$ 1,630</b>	<b>0.72%</b>	<b>100.00%</b>	<b>\$ 1,695</b>	<b>0.74%</b>	<b>100.00%</b>

- (1) Excludes loans held for sale.
- (2) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.
- (3) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.
- (4) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.

(This table is continued on the next page.)



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(Continued from the previous page.)

December 31,						
2004			2003			
Allowance for Loan Losses	Allocated Allowance as a % of Loan Category	Loan Category as a % of Total Loans <sup>(1)</sup>	Allowance for Loan Losses	Allocated Allowance as a % of Loan Category	Loan Category as a % of Total Loans <sup>(1)</sup>	
(dollars in millions)						
Allocated allowance:						
Loans secured by real estate:						
Home loans <sup>(2)</sup>	\$ 214	0.19%	53.10%	\$ 321	0.32%	57.12%
Home equity loans and lines of credit <sup>(2)</sup>	83	0.19	21.08	82	0.30	15.78
Subprime mortgage channel <sup>(3)</sup>	243	1.27	9.26	84	0.65	7.41
Home construction <sup>(4)</sup>	12	0.51	1.13	18	0.81	1.27
Multi-family	101	0.45	10.76	139	0.68	11.60
Other real estate	116	2.05	2.74	110	1.65	3.80
Total allocated allowance secured by real estate	769	0.38	98.07	754	0.44	96.98
Consumer:						
Credit card						
Other	36	4.55	0.38	49	4.77	0.59
Commercial	51	1.59	1.55	72	1.69	2.43
Total allocated allowance held in portfolio	856	0.41	100.00	875	0.50	100.00
Unallocated allowance	445	0.22		375	0.21	
Total allowance for loan losses	\$ 1,301	0.63%	100.00%	\$ 1,250	0.71%	100.00%

(1) Excludes loans held for sale.

(2) Excludes home loans and home equity loans and lines of credit in the subprime mortgage channel.

(3) Represents mortgage loans purchased from recognized subprime lenders and mortgage loans originated under the Long Beach Mortgage name and held in the investment portfolio.

(4) Represents loans to builders for the purpose of financing the acquisition, development and construction of single-family residences for sale and construction loans made directly to the intended occupant of a single-family residence.

As part of its ongoing program of model improvement, the Company introduced a new model to estimate incurred losses on multi-family loans in 2006. The new model uses a formulaic statistical-based approach for determining loss factors based on relevant default-predictive variables such as loan-to-value and debt service coverage ratios, and geographic factors. The model that was replaced used the same underlying classes of inputs but categorized loans for collective review using the risk grade assigned to them for bank regulatory purposes, the categorization of which inherently involved management judgment. The Company expects this new methodology to result in a better estimate of incurred loss, with greater consistency across periods; it is also more consistent with risk assessment practices in the commercial lending industry.

The allocated allowance for loan losses for home loans decreased \$20 million in 2006, while the allowance increased as a percentage of the total loan balance from 0.19% at the end of 2005 to 0.20% at the end of 2006. The \$20 million decrease in the allowance for home loans is a small amount relative to the approximately \$99 billion in the home loans portfolio at December 31, 2006. This decrease resulted from a combination of offsetting effects, including a \$15 billion decline in home loans balances during 2006. In addition, the credit risk profile of the loans remaining in the home loans held in portfolio also changed as home prices in geographic areas of portfolio concentration (e.g., California)

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generally appreciated over the course of 2006. Partially offsetting these factors that reduced the allocated allowance was the impact from increased levels of delinquencies and nonperforming assets.

The allocated allowance for loan losses for subprime mortgage channel loans decreased \$48 million in 2006 primarily due to the change in the estimate of the loss confirmation period from four years to



three years. The loss confirmation period represents the period between a loan default event occurring and the point at which the Company has knowledge of those events. Generally, borrowers are impacted by events that result in loan default and eventual loss well in advance of a lender's knowledge of those events. Examples of such loss-causing events for home loans are borrower job loss, divorce and medical crisis. The impact of changing the loss confirmation period was partially offset by an increase in the allowance for loan losses from improvements in the estimation of incurred losses associated with the Long Beach subprime portfolio with regard to loans with high loan-to-value ratios and loans in a junior lien position.

#### **90 or More Days Past Due and Still Accruing**

The total amount of loans held in portfolio, excluding credit card loans, that were 90 days or more contractually past due and still accruing interest was \$98 million, \$97 million, \$107 million, \$85 million and \$46 million at December 31, 2007, 2006, 2005, 2004 and 2003. The majority of these loans are either VA- or FHA-insured with little or no risk of loss of principal or interest. Managed credit card loans that were 90 days or more contractually past due and still accruing interest were \$836 million, \$586 million and \$465 million at December 31, 2007, 2006 and 2005, including \$174 million, \$113 million and \$87 million related to loans held in portfolio. The delinquency rate on managed credit card loans that were 30 days or more delinquent at December 31, 2007, 2006 and 2005 was 6.47%, 5.25% and 5.07%.

Delinquent mortgages contained within GNMA servicing pools that were repurchased or were eligible to be repurchased by the Company are reported as loans held for sale. Substantially all of these loans are either guaranteed or insured by agencies of the federal government and therefore do not expose the Company to significant risk of credit loss. Due to the sale of substantially all of the Company's government loan servicing portfolio in July 2006, the balance of such loans declined considerably. The Company's held for sale portfolio contained zero, \$37 million, \$1.06 billion, \$1.60 billion and \$2.50 billion of such loans that were 90 days or more contractually past due and still accruing interest at December 31, 2007, 2006, 2005, 2004 and 2003.

#### **Derivative Counterparty Credit Risk**

Derivative financial instruments expose the Company to credit risk in the event of nonperformance by counterparties to such agreements. This risk consists primarily of the termination value of agreements where the Company is in a favorable position. Credit risk related to derivative financial instruments is considered within the fair value measurement of the instrument. The Company manages the credit risk associated with its various derivative agreements through counterparty credit review, counterparty exposure limits and monitoring procedures. The Company obtains collateral from certain counterparties for amounts in excess of exposure limits and monitors all exposure and collateral requirements daily. The fair value of collateral received from a counterparty is continually monitored and the Company may request additional collateral from counterparties or return collateral pledged as deemed appropriate. The Company's agreements generally include master netting agreements whereby the counterparties are entitled to settle their positions "net." At December 31, 2007 and 2006, the gross positive fair value of the Company's derivative financial instruments was \$2.04 billion and \$618 million. The Company's master netting agreements at December 31, 2007 and 2006 reduced the exposure to this gross positive fair value by \$331 million and \$339 million. The Company's collateral against derivative financial instruments was \$1.28 billion and \$16 million at December 31, 2007 and 2006. Accordingly, the Company's net exposure to derivative counterparty credit risk at December 31, 2007 and 2006 was \$435 million and \$263 million.

## **Liquidity Risk and Capital Management**

### **Liquidity Risk**

The objective of liquidity risk management is to ensure that the Company has the continuing ability to maintain cash flows that are adequate to fund operations and meet its other obligations on a timely and cost-effective basis in various market conditions. Changes in market conditions, the composition of its balance sheet and risk tolerance levels are among the factors that influence the Company's liquidity profile. The Company establishes liquidity guidelines for the Parent as well as for its banking subsidiaries.

The Parent and its banking subsidiaries have separate liquidity risk management policies and contingent funding plans as each has different funding needs and requirements and sources of liquidity. The Company's banking subsidiaries also have regulatory capital requirements. The Company has policies that require current and forecasted liquidity positions to be monitored against pre-established limits and requires that contingency liquidity plans be maintained.

For the Company's banking subsidiaries, liquidity is forecasted over short term (operational) and long term (strategic) horizons. Both approaches require that the Company's banking subsidiaries maintain minimum amounts of liquidity that exceed forecasted needs (excess liquidity). Whereas the focus for operational liquidity is to maintain sufficient excess liquidity to satisfy unanticipated funding requirements, strategic liquidity focuses on stress-testing liquidity risks and ensuring that sufficient excess liquidity is maintained under various scenarios to meet policy standards.

#### *Parent*

The Parent's primary sources of liquidity are dividends from subsidiaries and funds raised in various capital markets. Dividends paid by the Parent's banking subsidiaries may fluctuate from time to time in order to ensure that both internal capital targets and various regulatory requirements related to capital adequacy are met. For more information on dividend limitations applicable to the Parent's banking subsidiaries, refer to "Business Regulation and Supervision" and Note 20 to the Consolidated Financial Statements "Regulatory Capital Requirements and Dividend Restrictions."

In January 2006, the Parent filed an automatically effective registration statement under which an unlimited amount of debt securities, preferred stock and depositary shares were registered. The Parent's long-term and short-term indebtedness are rated A- and F2 by Fitch, BBB+ and A2 by Standard & Poor's, Baa2 and P2 by Moody's, and AL and R-1L by DBRS.

#### *Banking Subsidiaries*

The principal sources of liquidity for the Parent's banking subsidiaries are retail deposits, FHLB advances, repurchase agreements, federal funds purchased, the maturity and repayment of portfolio loans, securities held in the available-for-sale portfolio and loans designated as held for sale. Retail deposits continue to provide the Company with a significant source of stable funding while FHLB advances have increased in importance in the second half of 2007. The Company's continuing ability to retain its retail deposit base and to attract new deposits depends on various factors such as customer service satisfaction levels and the competitiveness of interest rates offered on deposit products. Washington Mutual Bank continues to have the necessary assets available to pledge as collateral for additional FHLB advances, repurchase agreements and other collateral-dependent sources of liquidity.

FHLB borrowings have always been an important source of liquidity for the Company and remain so today. In response to the current global credit crisis, decreased investor risk tolerance levels and near-evaporation of liquidity in the secondary markets, the Parent's banking subsidiaries increased their borrowings from the Federal Home Loan Bank system in the second half of 2007. The increase in FHLB borrowings by \$42.44 billion from June 30, 2007 or \$19.56 billion from December 31, 2006 was

facilitated by the \$47.36 billion reduction in FHLB borrowings over the 18 months prior to June 30, 2007 as the Company diversified its wholesale funding sources and reduced the size of its balance sheet.

For the year ended December 31, 2007, proceeds from the sale of loans originated and held for sale were approximately \$78.93 billion. These proceeds were, in turn, used as the primary funding source for the origination and purchase, net of principal payments, of approximately \$77.38 billion of loans held for sale during the same period.

While recent market events have impacted the Company's liquidity planning, the Company remains comfortable with its ability to fund its mortgage banking operations. The Company's liquidity planning assumes that the only reliable sources of liquidity in the secondary mortgage market are Fannie Mae and Freddie Mac. While turbulence in the secondary mortgage market may change the type of liquidity the Company accesses, the amount of funding that is necessary to sustain the Company's mortgage banking operations does not typically affect overall liquidity levels.

As part of its funding diversification strategy, Washington Mutual Bank launched a €20 billion covered bond program in September 2006. While €14 billion remains unissued under this program, no further issuances may occur until the Company's credit ratings assigned by Moody's are upgraded or the ratings-based restrictions are eliminated. Existing floating-rate U.S. dollar-denominated mortgage bonds were issued by Washington Mutual Bank and collateralize the outstanding Euro-denominated covered bonds. The covered bonds were issued by a statutory trust that is not consolidated by the Company. The mortgage bonds are secured principally by residential mortgage loans in Washington Mutual Bank's portfolio.

Under the Global Bank Note Program, which was established in August 2003 and renewed in December 2005, Washington Mutual Bank may issue senior and subordinated notes in the United States and in international capital markets in a variety of currencies and structures. Washington Mutual Bank had \$12.44 billion available under this program as of December 31, 2007.

Senior unsecured long-term obligations of Washington Mutual Bank are rated A- by Fitch, A- by Standard & Poor's, Baa1 by Moody's and A by DBRS. Short-term obligations are rated F2 by Fitch, A2 by Standard & Poor's, P2 by Moody's and R-1L by DBRS.

### **Capital Management**

The Company monitors capital adequacy for both the Company (on a consolidated basis) and its regulated banking subsidiaries. Sufficient capital is maintained at both levels to provide for unexpected losses based on the risks inherent in the combination of businesses. The views of investors, credit rating agencies, lenders and regulators are considered in determining capital ratio targets.

Capital is generated through the Company's business operations and through issuance of capital securities such as common stock and perpetual preferred stock, and the Company's capital management program promotes the efficient use of these resources. Capital is primarily used to fund organic growth, pay dividends and repurchase shares. On a consolidated basis, capital may also be raised through issuance of capital securities by various subsidiaries of the Company and its banking subsidiaries, in particular Washington Mutual Preferred Funding LLC ("WMPF LLC").

During 2007, the Company issued approximately \$1.5 billion of perpetual, non-cumulative preferred securities through its indirect subsidiary, WMPF LLC. While the high equity content characteristics of these securities have long been acknowledged by the OTS as qualifying elements in the composition of financial institutions' core capital structures, the rating agencies have only recently taken a similar view. Accordingly, such securities are included as equity components within the Company's tangible equity to total tangible assets ratio, estimated Tier 1 leverage ratio, and estimated total risk-based capital ratio.

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Additionally, in the fourth quarter of 2007, the Company issued \$3.0 billion of Series R Non-Cumulative Perpetual Convertible Preferred Stock for net proceeds of approximately \$2.9 billion. Of the total net proceeds received from the sale of Series R Preferred Stock, \$1.0 billion was contributed to the Company's banking subsidiary, Washington Mutual Bank, to enhance its capital position as it manages anticipated heightened credit losses. The remaining proceeds have been retained at the Company to enhance its liquidity profile and eliminate the need for dividend flows to support anticipated cash flows through the next two years.

The Company's ability to generate capital internally through earnings was significantly impacted in 2007 by the deteriorating credit environment. With early indicators in 2008 suggesting that the housing market continues to deteriorate, the Company expects that it will continue to experience significantly higher credit costs throughout its single-family residential mortgage portfolios, which will in turn significantly impact the Company's ability to generate capital internally through earnings. Management has taken steps to mitigate the capital impact of the current earnings outlook by recommending that the Company's Board of Directors reduce the quarterly dividend payment to common stockholders to 15 cents per share from the prior level of 56 cents per share it paid in the fourth quarter. Management has incorporated this new reduced level of dividends into its capital and liquidity forecasts for 2008. Refer to Item 1A Risk Factors for additional information regarding risks related to capital sufficiency.

On January 15, 2008, the Company's Board of Directors declared a cash dividend of 15 cents per share on the Company's common stock, payable on February 15, 2008 to shareholders of record as of January 31, 2008. The Company's Board of Directors considers a variety of factors when determining the dividend on the Company's common stock, including overall capital levels, liquidity position and the Company's earnings. In addition, the Company will pay a dividend of 36 cents per depositary share of Series K Preferred Stock, and a dividend of \$19.16 per share of Series R Preferred Stock on March 17, 2008 to shareholders of record on March 3, 2008.

With certain limited exceptions, if the Company does not pay full quarterly dividends on any issued and outstanding class or series of its preferred stock for a particular dividend period, then the Company may not pay dividends on, or repurchase, redeem or make a liquidation payment with respect to its common stock or other junior securities during the next succeeding dividend period. Refer to Note 17 to the Consolidated Financial Statements "Preferred Stock and Minority Interest" for additional information.

As part of its capital management activities, from time to time the Company has repurchased shares to deploy excess capital. The Company adopted a new share repurchase program approved by the Board of Directors in 2006 (the "2006 Program"). Under the 2006 Program, the Company is authorized to repurchase up to 150 million shares of its common stock, as conditions warrant. There is no fixed termination date for the 2006 Program and purchases may be made in the open market, through block trades, accelerated share repurchase transactions, private transactions, or otherwise. Recently, the Company has focused on capital retention, and has not engaged in share repurchase activities since the third quarter of 2007. The total remaining common stock repurchase authority under the 2006 Program was 47.5 million shares as of December 31, 2007.

When the Company engages in share repurchases, management evaluates the relative risks and benefits of repurchasing shares in the open market, with the attendant daily trading limits and other constraints of the SEC Rule 10b-18 safe harbor, as compared with an accelerated share repurchase ("ASR") transaction. In an ASR transaction, the Company repurchases a large block of stock at an initial specified price from a counterparty, typically a large broker-dealer, who has borrowed the shares. Upon final settlement of an ASR transaction, the initial specified price is adjusted to reflect actual prices at which the Company's shares traded over the period of time after the initial repurchase that is specified in the ASR agreement. Through this final settlement process, market risks and costs

associated with fluctuations in the Company's stock price during the subsequent time period may be transferred from the counterparty to the Company.

ASR transactions immediately deploy the capital associated with share repurchases, making them economically more efficient than open market repurchases. Additionally, ASR transactions may be structured to include optionality or hedging arrangements that afford the Company the opportunity to mitigate price risk, and potentially mitigate the volatility of open market price fluctuations. While these benefits of an ASR transaction are significant considerations, open market repurchases are usually a more operationally efficient alternative when the Company chooses to deploy its excess capital in smaller amounts, particularly given the time required and the complexity associated with structuring an ASR transaction. In contrast, when the Company chooses to deploy its excess capital in larger amounts, an ASR transaction becomes more attractive and shares repurchased in an ASR transaction are removed upon the initiation of the repurchase when calculating earnings per share. Because ASR transactions involve more complex legal structures and counterparty risks than open market repurchases, the Company retains outside legal counsel to assist in structuring and documenting the transactions and applies its market risk and counterparty credit risk management standards. Additional information regarding these transactions is included in Note 16 to the Consolidated Financial Statements "Common Stock."

Refer to Item 5 "Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities" for additional information regarding share repurchase activities.

### Capital Composition and Capital Ratios

The Parent's core capital consists primarily of common and preferred stock, retained earnings and, to a lesser degree, trust preferred securities. In recent years, the Company has remixed its core capital by replacing some of its common stock and trust preferred securities with perpetual non-cumulative preferred stock that reduced the cost of capital while preserving its core capital quality as shown below:

	At December 31,		
	2007	2006	2005
	(in millions)		
Capital Surplus-Common Stock	\$ 2,630	\$ 5,825	\$ 8,176
Series K Preferred Stock	492	492	
Series R Preferred Stock	2,900		
WMPF LLC Preferred Securities	3,912	2,446	
Trust Preferred Securities	813	1,880	1,795

OTS capital guidelines require that the dominant form of a savings association's equity (referred to as "core capital" under OTS guidelines, and equivalent to Tier 1 capital for other banking institutions) should be common voting shares and that savings associations should avoid undue reliance on preferred securities. Preferred securities issued by WMPF LLC (an indirect subsidiary of WMB) qualify as Tier 1 (core) capital at WMB. As a prudent safeguard, OTS limits the amount of WMB's Tier 1 (core) capital that may be comprised of preferred securities to an amount that cannot exceed 25% of its Tier 1 capital. At December 31, 2007, the aggregate amount of preferred securities issued by WMPF LLC totaled approximately \$3.91 billion (net of expense) which represents 17.5% of its \$22.4 billion Tier 1 (core) capital. In 2007, WMB also redeemed \$170 million of preferred stock. WMBfsb's capital structure does not contain any preferred securities.

The Parent is not required by the OTS to report its capital ratios, and as the Parent is not a bank holding company it is not required by the Federal Reserve Board to report its capital ratios. Nevertheless, capital ratios are integral to the Company's capital management process and the provision of such metrics facilitates peer comparisons with Federal Reserve Board-regulated bank holding companies. The ratio for the Company's tangible equity to total tangible assets, along with the

estimated ratios for Tier 1 capital to average total assets and total risk-based capital to total risk-weighted assets which exceed minimum regulatory guidelines, are presented below.

	At December 31,	
	2007	2006
(dollars in millions)		
Tangible equity	\$ 21,387	\$ 20,374
Total tangible assets	320,749	337,050
Tangible equity to total tangible assets	6.67%	6.04%
Tier 1 capital	\$ 21,610	\$ 21,789
Average total assets	315,832	343,178
Tier 1 leverage	6.84%	6.35%
Total risk-based capital	\$ 31,128	\$ 30,068
Total risk-weighted assets	252,330	255,450
Total risk-based capital to total risk-weighted assets	12.34%	11.77%

*Subsidiary capital requirements*

The regulatory capital ratios of Washington Mutual Bank and Washington Mutual Bank fsb and minimum regulatory capital ratios to be categorized as well-capitalized are included in Note 20 to the Consolidated Financial Statements "Regulatory Capital Requirements and Dividend Restrictions."

The Company's broker-dealer subsidiaries are also subject to capital requirements. At December 31, 2007 and 2006, all of its broker-dealer subsidiaries were in compliance with their applicable capital requirements. During December 2007, the Company announced its intention to close WCC, its institutional broker-dealer business. In January 2008, substantially all the holdings of WCC were sold to various other subsidiaries of the Company in arms-length transactions.

**Market Risk Management**

Market risk is defined as the sensitivity of income, fair market values and capital to changes in interest rates, foreign currency exchange rates, commodity prices and other relevant market rates or prices. The primary market risk to which the Company is exposed is interest rate risk. Substantially all of its interest rate risk arises from instruments, positions and transactions entered into for purposes other than trading. These include loans, MSR, securities, deposits, borrowings, long-term debt and derivative financial instruments.

The Company's trading assets are primarily comprised of financial instruments that are retained from securitization transactions, or are purchased for MSR risk management purposes. The Company does not take significant short-term trading positions for the purpose of benefiting from price differences between financial instruments and markets.

From time to time the Company issues debt denominated in foreign currencies. When such transactions occur, the Company uses derivatives to offset the associated foreign currency exchange risk.

Interest rate risk is managed within a consolidated enterprise risk management framework that includes asset/liability management and the management of specific portfolios (MSR and Other Mortgage Banking) discussed below. The principal objective of asset/liability management is to manage the sensitivity of net income to changing interest rates. Asset/liability management is governed by a policy reviewed and approved annually by the Board. The Board has delegated the oversight of the administration of this policy to the Finance Committee of the Board.

### **Types of Interest Rate Risk**

The Company is exposed to different types of interest rate risks. These include lag, repricing, basis, prepayment, lifetime and periodic payment caps, and volatility risk.

#### *Lag/Repricing Risk*

Lag risk results from timing differences between the repricing of adjustable-rate assets and liabilities. Repricing risk is caused by the mismatch in the maturities between assets and liabilities. For example, the Company's assets may reprice slower than its liabilities. The effect of this timing difference, or "lag," will generally be favorable during a period of declining interest rates and unfavorable during a period of rising interest rates. Lag/repricing risk can produce short-term volatility in net interest income during periods of interest rate movements, but the effect of this lag generally balances out over time.

#### *Basis Risk*

Basis risk occurs when assets and liabilities have similar repricing frequencies but are tied to different market interest rate indices. For example, adjustable-rate loans may reprice based on Treasury rates while borrowings may reprice based on LIBOR rates.

#### *Prepayment Risk*

Prepayment risk results from the ability of customers to pay off their loans prior to maturity. Generally, prepayments increase in falling interest rate environments and decrease in rising interest rate environments.

#### *Lifetime and Periodic Payment Cap Risk*

Many of the Company's adjustable-rate home loan products contain lifetime interest rate caps, which prevent the interest rate on the loan from exceeding a contractually determined level. In periods of dramatically rising rates, those adjustable-rate loans that have reached their lifetime cap rate will no longer reprice upward. Periodic payment caps limit the amount that a borrower's scheduled payment on an adjustable-rate loan can increase when the interest rate is adjusted upward on the loan's periodic repricing date.

#### *Volatility Risk*

Volatility risk is the potential change in the fair value of an option, or a fixed income instrument containing options (such as mortgages) from changes in the implied market level of future volatility ("implied volatility"). For the holder of an option contract, implied volatility is a key determinant of option value with higher volatility generally increasing option value and lower volatility generally decreasing option value.

### **MSR Risk Management**

The Company manages potential changes in the fair value of MSR through a comprehensive risk management program. The intent is to mitigate the effects of changes in MSR fair value through the use of risk management instruments. Risk management instruments may include interest rate contracts, forward rate agreements, forward purchase commitments and available-for-sale and trading securities. The securities generally consist of fixed-rate debt securities, such as U.S. Government and agency obligations and mortgage-backed securities, including principal-only strips. The interest rate contracts typically consist of interest rate swaps, interest rate swaptions, interest rate futures and interest rate caps and floors. The Company may purchase or sell option contracts, depending on the portfolio risks

it seeks to manage. The Company also enters into forward commitments to purchase and sell mortgage-backed securities, which generally are comprised of fixed-rate mortgage-backed securities with 15 or 30 year maturities.

The fair value of MSR is primarily affected by changes in expected prepayments that result from changes in spot and future primary mortgage rates and in changes in other applicable market interest rates. Changes in the value of MSR risk management instruments vary based on the specific instrument. For example, changes in the fair value of interest rate swaps are driven by shifts in interest rate swap rates and the fair value of U.S. Treasury securities is based on changes in U.S. Treasury rates. Mortgage rates may move more or less than the rates on Treasury bonds or interest rate swaps. This could result in a change in the fair value of the MSR that differs from the change in fair value of the MSR risk management instruments. Potential differences in the change in value between MSR and MSR risk management instruments are what is referred to as basis risk.

The Company manages the MSR daily and adjusts the mix of instruments used to offset MSR fair value changes as interest rates and market conditions warrant. The objective is to maintain an efficient and fairly liquid mix as well as a diverse portfolio of risk management instruments with maturity ranges that correspond well to the anticipated behavior of the MSR. The Company also manages the size of the MSR asset, such as through the structuring of servicing agreements when loans are sold, and by periodically selling or purchasing servicing assets.

In June 2007, the Company changed the model used to estimate the fair value of substantially all of its MSR from a static valuation model to an option-adjusted spread ("OAS") valuation model. The OAS model projects MSR cash flows over multiple interest rate scenarios, and discounts these cash flows using risk-adjusted discount rates. The significant assumptions used in the valuation of MSR include market interest rates, projected prepayment speeds, cost to service, ancillary income and option-adjusted spreads. Additionally, an independent broker estimate of the fair values of the mortgage servicing rights is obtained quarterly along with other market-based evidence. Management uses this information together with its OAS valuation methodology to estimate the fair value of the MSR.

The Company believes this overall risk management strategy is the most efficient approach to managing MSR fair value risk. The success of this strategy, however, is dependent on management's decisions regarding the amount, type and mix of MSR risk management instruments that are selected to manage the changes in fair value of the mortgage servicing asset. If this strategy is not successful, net income could be adversely affected.

#### **Other Mortgage Banking Risk Management**

The Company also manages the risks associated with its home loan mortgage warehouse and pipeline. The mortgage warehouse consists of funded loans intended for sale in the secondary market. The pipeline consists of commitments to originate or purchase mortgages to be sold in the secondary market. The interest rate risk associated with the mortgage pipeline and warehouse is the potential for changes in interest rates between the time the customer locks in the rate on the loan and the time the loan is sold.

The Company measures the risk profile of the mortgage warehouse and pipeline daily. To manage the warehouse and pipeline risk, management executes forward sales commitments, interest rate contracts and mortgage option contracts. A forward sales commitment protects against a rising interest rate environment, since the sales price and delivery date are already established. A forward sales commitment is different, however, from an option contract in that the Company is obligated to deliver the loan to the third party on the agreed-upon future date. Management also estimates the fallout factor, which represents the percentage of loans that are not expected to be funded, when determining the appropriate amount of pipeline risk management instruments.



### Asset/Liability Risk Management

The purpose of asset/liability risk management is to assess the aggregate interest rate risk profile of the Company. Asset/liability risk analysis combines the MSR and Other Mortgage Banking activities with substantially all of the other remaining interest rate risk positions inherent in the Company's operations.

To analyze interest rate risk sensitivity, management projects net interest income under a variety of interest rate scenarios, assuming both parallel and non-parallel shifts in the yield curve. These scenarios illustrate net interest income sensitivity due to changes in the level of interest rates, the slope of the yield curve and the spread between Treasury and LIBOR/swap ("LIBOR") rates. Management also periodically projects the interest rate sensitivity of net income due to changes in the level of interest rates. Additionally, management projects the discounted value of assets and liabilities under different interest rate scenarios to assess their risk exposure over longer periods of time.

The projection of the sensitivity of net income, net interest income and discounted cash flow analyses requires numerous assumptions. Prepayment speeds, decay rates (the estimated runoff of deposit accounts that do not have a stated maturity), future deposits and loan rates and loan and deposit volume and mix projections are among the most significant assumptions. Prepayments affect the size of the loan and mortgage-backed securities portfolios, which impacts net interest income. All deposit and loan portfolio assumptions, including loan prepayment speeds and deposit decay rates, require management's judgments of anticipated customer behavior in various interest rate environments. These assumptions are derived from internal and external analyses. The rates on new investment securities and borrowings are estimated based on market rates while the rates on deposits and loans are estimated based on the rates offered by the Company to retail customers.

The slope of the yield curve, current interest rate conditions and the speed of changes in interest rates all affect sensitivity to changes in interest rates. Short-term borrowings and, to a lesser extent, interest-bearing deposits typically reprice faster than the Company's adjustable-rate assets. This lag effect is inherent in adjustable-rate loans and mortgage-backed securities indexed to the 12-month average of the annual yields on actively traded U.S. Treasury securities adjusted to a constant maturity of one year and those indexed to the 11<sup>th</sup> District FHLB monthly weighted-average cost of funds index.

The sensitivity of new loan volume and mix to changes in market interest rate levels is also projected. Management generally assumes a reduction in total loan production in rising interest rate scenarios accompanied by a shift towards a greater proportion of adjustable-rate production. Conversely, the Company generally assumes an increase in total loan production in falling interest rate scenarios accompanied by a shift towards a greater proportion of fixed-rate loans. The gain from mortgage loans also varies under different interest rate scenarios. Normally, the gain from mortgage loans increases in falling interest rate environments primarily from an increase in mortgage refinancing activity. Conversely, the gain from mortgage loans may decline when interest rates increase if management chooses to retain more loans in the portfolio.

In periods of rising interest rates, the net interest margin normally contracts since the repricing period of the Company's liabilities is shorter than the repricing period of its assets. The net interest margin generally expands in periods of falling interest rates as borrowing costs reprice downward faster than asset yields.

To manage interest rate sensitivity, management utilizes the interest rate risk characteristics of the balance sheet assets and liabilities to offset each other as much as possible. Balance sheet products have a variety of risk profiles and sensitivities. Some of the components of interest rate risk are countercyclical. Management may adjust the amount or mix of risk management instruments based on the countercyclical behavior of the balance sheet products.

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When the countercyclical behavior inherent in portions of the Company's balance sheet does not result in an acceptable risk profile, management utilizes investment securities and interest rate contracts to mitigate this situation. The interest rate contracts used for this purpose are classified as asset/liability risk management instruments. These contracts are often used to modify the repricing period of interest-bearing funding sources with the intention of reducing the volatility of net interest income. The types of contracts used for this purpose may consist of interest rate swaps, interest rate corridors, interest rate swaptions and certain derivatives that are embedded in borrowings. Management also uses receive-fixed swaps as part of the asset/liability risk management strategy to help modify the repricing characteristics of certain long-term liabilities to match those of the assets. Typically, these are swaps of long-term fixed-rate debt to a short-term adjustable-rate, which more closely resembles asset repricing characteristics.

### January 1, 2008 and January 1, 2007 Net Interest Income Sensitivity Comparison

The table below indicates the sensitivity of net interest income as a result of hypothetical interest rate movements on market risk sensitive instruments. The base case assumptions used for this sensitivity analysis are similar to the Company's most recent net interest income projection for the respective twelve month periods as of the date the analysis was performed. The comparative results assume parallel shifts in the yield curve with interest rates rising 100 basis points and decreasing 100 basis points in even quarterly increments over the twelve month periods ending December 31, 2008 and December 31, 2007.

Commencing with the analysis for the one year period beginning January 1, 2008, the interest rate scenarios will be derived from the year end forward yield curve. The comparative analysis is presented based on current coupon rates while the net interest income sensitivity based on the forward yield curve is presented separately. The revision to the interest rate scenario more closely aligns the analysis with market expectations. The base scenario for the current coupon rate analysis were the market rates as of December 31 held constant for the next twelve months. The base scenario for the implied forward rate analysis represents market expectations for interest rates for the next twelve months. The parallel scenarios represent the same absolute change in interest rates in both analyses.

These analyses also incorporate assumptions about balance sheet dynamics such as loan and deposit growth and pricing, changes in funding mix and asset and liability repricing and maturity characteristics. The projected interest rate sensitivities of net interest income shown below may differ significantly from actual results, particularly with respect to non-parallel shifts in the yield curve or changes in the spreads between mortgage, Treasury and LIBOR rates, changes in loan volumes or loan and deposit pricing.

### Comparative Net Interest Income Sensitivity

	Gradual Change in Rates	
	-100 basis points	+100 basis points
<b>Current coupon rates</b>		
Net interest income change for the one year period beginning:		
January 1, 2008	3.13%	(2.67)%
January 1, 2007	3.80	(3.04)
Gradual Change in Rates		
	-100 basis points	+100 basis points
<b>Implied forward rates</b>		
Net interest income change for the one year period beginning:		
January 1, 2008	2.78%	(2.74)%

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Treasury and LIBOR rates in the January 1, 2008 net interest income sensitivity analyses were lower than the rates at January 1, 2007 with Treasury rates declining significantly more than LIBOR rates. At January 1, 2008, two year interest rates were lower than three month and ten year interest rates on the Treasury and LIBOR curves. The January 1, 2007 curve was inverted with three month rates higher than ten year rates. The shape of the curves contributes to a continuing challenging interest rate environment for the Company.

Net interest income sensitivity declined in the  $\pm 100$  basis point environments in the January 1, 2008 analysis compared to the January 1, 2007 analysis. The main factors contributing to the reduction in sensitivity was the execution of term fixed-rate funding and interest rate contracts and changes in the projected balance sheet during the subsequent twelve month periods. The term funding and interest rate contracts were executed to offset the increased sensitivity resulting from the retention of medium-term adjustable-rate loans during the second half of 2007. A reduction in projected prepayments and loan volume resulted in decreased changes in average earning assets in all scenarios. The net result was a decreased change in net interest income in the  $\pm 100$  basis point environments, as compared to the January 1, 2007 analysis.

The net interest income sensitivity in the -100 basis point scenario in the implied forward rates analysis was slightly lower than in the current coupon rates analysis primarily due to enhanced net interest income in the base scenario. Net interest income increased in the base implied forward rates analysis as the projected interest rates were lower.

### **January 1, 2008 and January 1, 2007 Net Income Sensitivity Comparison**

Similar to the net interest income sensitivity analysis, management also periodically projects net income in a variety of interest rate scenarios assuming parallel shifts in the yield curve. The net income simulations project changes in MSR and related hedges, all of which are carried at fair value and whose values are sensitive to changes in interest rates. The analysis assumes no changes in credit provisions, gain on sale, non-interest income or non-interest expense except for the fair value changes in MSR and related hedges.

In performing net income simulations, parallel shifts in the yield curve are assumed, with interest rates rising 100 basis points and decreasing 100 basis points in even quarterly increments over the twelve month periods ending December 31, 2008 and 2007. The interest rate scenarios are identical to the scenarios used for the net interest income comparison. The assumptions used in the base scenario are similar to the assumptions used in the Company's most current earnings forecast.

For the twelve month period ending December 31, 2008, using current coupon rates, net income is projected to increase approximately \$170 million in the -100 basis point simulation while it is projected to decrease approximately \$110 million in the +100 basis point simulation. In comparison, net income was projected to increase approximately \$70 million in the -100 basis point scenario and decrease approximately \$100 million in the +100 basis point scenario for the twelve month period ended December 31, 2007. For the twelve month period ending December 31, 2008, using implied forward rates, net income is projected to increase approximately \$160 million in the -100 basis point simulation while it is projected to decrease approximately \$120 million in the +100 basis point simulation. The differences in the results between the implied forward curve rates and the current coupon rates analysis was due to slight variances in net interest income sensitivity offset by changes in the performance of MSR and related hedges.

The projected increase in net income in the -100 basis point scenario for the twelve month period ending December 31, 2008 was mainly due to an improvement in other income (fair value changes in the MSR and related hedges) offset by less of an increase in net interest income. Net income in the +100 basis point environment was similar, as an improvement in other income was offset by less of a decrease in net interest income. This was mainly due to a reduction in projected MSR

unpaid principal balances and changes in the shape of the yield curve resulting in changes to the projected hedging costs. The reduction in MSR unpaid principal balances was due to expected decreases in loan sales during the twelve month forecast resulting from changes in the secondary mortgage market.

These net income and net interest income sensitivity analyses are limited in that they were performed at a particular point in time and do not reflect certain factors that would impact the Company's financial performance in a changing interest rate environment. Most significantly, the impact of changes in gain on sale from mortgage loans that result from changes in interest rates is not modeled in the simulation. The net income and net interest income analyses also assume no changes in credit spreads. In addition, the net income sensitivity analysis assumes no changes in credit provisions, noninterest income or noninterest expense in the different scenarios other than changes in the fair value of MSR and related hedges. Additional provisions may be required in a falling interest rate scenario while fewer provisions may be necessary in a rising rate scenario substantially changing the projected net income sensitivity estimates. The analyses assume management does not initiate additional strategic actions, such as increasing or decreasing term funding or selling assets, to offset the impact of projected changes in net interest income or net income in these scenarios.

The analyses are also dependent on the reliability of various assumptions used, including prepayment forecasts and discount rates, and do not incorporate other factors that would impact the Company's overall financial performance in such scenarios. These analyses also assume that the projected MSR risk management strategy is effectively implemented and that mortgage and interest rate swap spreads are constant in all interest rate environments. These assumptions may not be realized. For example, changes in spreads between interest rate indices could result in significant changes in projected net income sensitivity. Projected net income may increase if market rates on interest rate swaps decrease by more than the decrease in mortgage rates, while the projected net income may decline if the rates on swaps increase by more than mortgage rates. Accordingly, the preceding sensitivity estimates should not be viewed as an earnings forecast.

### **Operational Risk Management**

Operational risk is the risk of loss resulting from human fallibility, inadequate or failed internal processes or systems, or from external events, including loss related to legal risk. Operational risk can occur in any activity, function, or unit of the Company.

Primary responsibility for managing operational risk rests with the lines of business. Each line of business is responsible for identifying its operational risks and establishing and maintaining appropriate business-specific policies, internal control procedures and tools to quantify and monitor these risks. To help identify, assess and manage corporate-wide risks, the Company uses corporate support groups such as Legal, Compliance, Information Security, Continuity Assurance, Enterprise Spend Management and Finance. These groups assist the lines of business in the development and implementation of risk management practices specific to the needs of each business.

The Operational Risk Management Policy, approved by the Audit Committee of the Board of Directors, establishes the Company's operational risk framework and defines the roles and responsibilities for the management of operational risk. The operational risk framework consists of a methodology for identifying, measuring, monitoring and controlling operational risk combined with a governance process that complements the Company's organizational structure and risk management philosophy. The Operational Risk Committee ensures consistent communication and oversight of significant operational risk issues across the Company and ensures sufficient resources are allocated to maintain business-specific operational risk controls, policies and practices consistent with and in support of the operational risk framework and corporate standards.

The Operational Risk Management function, part of Enterprise Risk Management, is responsible for maintaining the framework and works with the lines of business and corporate support functions to ensure consistent and effective policies, practices, controls and monitoring tools for assessing and managing operational risk across the Company. The objective of the framework is to provide an integrated risk management approach that emphasizes proactive management of operational risk using measures, tools and techniques that are risk-focused and consistently applied company-wide. Such tools include the collection of internal operational loss event data, relevant external operational loss event data, results from scenario analysis, and assessments of the Company's business environment and internal control factors. These elements are used to determine the Company's operational risk profile and are included in the measurement of operational risk capital.

### **Tax Uncertainties**

The Company accounts for unrecognized income tax benefits in accordance with FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN 48"), which was adopted on January 1, 2007. FIN 48 requires that a tax benefit be recognized only if it is "more likely than not" that it will be realized, based solely on its technical merits, as of the reporting date. A tax position that meets the more-likely-than-not criterion shall be measured at the largest amount of benefit that is more than 50 percent likely of being realized upon settlement. As a result of the implementation of FIN 48, the Company recognized a \$6 million increase in the liability for unrecognized tax benefits, which was accounted for as a reduction to the January 1, 2007 balance of retained earnings.

Prior to January 1, 2007, the Company accounted for income and other tax contingencies in accordance with FASB Statement No. 5, *Accounting for Contingencies* ("FAS 5"). The calculation of tax liabilities under FAS 5 involves judgment in estimating the impact of uncertainties in the application of complex tax laws. The Company continues to account for non-income tax contingencies in accordance with FAS 5.

### **Goodwill Litigation**

On August 9, 1989, the Financial Institutions Reform, Recovery and Enforcement Act was enacted. Among other things, the Act raised the minimum capital requirements for savings institutions and required a phase-out of the amount of supervisory goodwill that could be included in satisfying certain regulatory capital requirements. The exclusion of supervisory goodwill from the regulatory capital of many savings institutions led them to take actions to replace the lost capital either by issuing new qualifying debt or equity securities or to reduce assets. A number of these institutions and their investors subsequently sued the United States Government seeking damages based on breach of contract and other theories (collectively "Goodwill Lawsuits").

To date, trials have been concluded and opinions have been issued in a number of Goodwill Lawsuits in the United States Court of Federal Claims. Generally, in Goodwill Lawsuits in which opinions have been issued by the Court of Federal Claims, either the plaintiffs, the defendant (U.S. Government), or both the plaintiffs and the defendant, have opted to appeal the decision to the United States Court of Appeals for the Federal Circuit. Typically, following completion of these appeals, one or more parties has petitioned the United States Supreme Court for a writ of certiorari, but all such petitions have been denied. Generally, the appeals have resulted in the cases being remanded to the Court of Federal Claims for further trial proceedings.

#### **American Savings Bank, F.A.**

In December 1992, American Savings Bank, Keystone Holdings, Inc. and certain related parties brought a lawsuit against the U.S. Government, alleging, among other things, that in connection with the acquisition of American Savings Bank they entered into a contract with agencies of the United

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States and that the U.S. Government breached that contract. As a result of the Keystone acquisition, the Company succeeded to all of the rights of American Savings Bank, Keystone Holdings and the related parties in such litigation and will receive any recovery from the litigation.

In connection with the Keystone acquisition, there are 6 million shares of the Company's common stock currently in escrow. In addition, as of December 31, 2007, the escrow included \$75.9 million in cash dividends paid on escrowed shares as well as interest accumulated on those dividends. Under the terms of the escrow arrangement, upon receipt of net cash proceeds from a final nonappealable judgment in or settlement of the litigation prior to the expiration of the escrow, one share (together with the dividends and interest attributable to such share) will be released from escrow to the Keystone investors for each \$18.4944 of net proceeds received by the Company. In September 2007, the escrow agreement was amended to extend the expiration date from December 20, 2008 to June 30, 2020. As a result of the amendment, in 2007, the Company received cash payments totaling \$17.2 million from the escrow. Additionally, the Company is entitled during 2008 to receive quarterly cash payments from the escrow, each in an amount equal to approximately 2% of the then value of the escrow. Thereafter, the Company is entitled to receive quarterly distributions from the escrow, each consisting of 130,435 shares of the Company's common stock and the dividends and interest then in the escrow attributable to such shares.

On December 18, 2006, a summary judgment order in favor of plaintiffs was entered in the lawsuit in the amount of \$402 million. On February 14, 2007, the U.S. Government filed a Notice of Appeal to the United States Court of Appeals for the Federal Circuit of that and several earlier trial court decisions. On December 7, 2007, the Court of Appeals heard oral argument and took the matter under advisement.

### **Dime Bancorp, Inc.**

In January 1995, Anchor Savings Bank FSB, filed suit against the U.S. Government for unspecified damages involving supervisory goodwill related to its acquisition of eight troubled savings institutions from 1982-1985. Four of the acquisitions involved financial assistance from the U.S. Government, and four did not. The Dime Savings Bank of New York, FSB acquired Anchor Savings Bank shortly after the case was brought and Dime Savings Bank assumed the rights under the litigation against the U.S. Government. Dime Bancorp distributed a Litigation Tracking Warrant (an "LTW") for each share of its common stock outstanding on December 22, 2000 to each of its shareholders on that date. In January 2002, Dime Savings Bank and Dime Bancorp merged into WMB and the Company. As a result of these mergers, the Company assumed the litigation against the U.S. Government and the LTWs are now, when exercisable, exercisable for shares of the Company's common stock. The events and conditions that would entitle a holder to exercise an LTW did not change as a result of these mergers and had not yet occurred as of December 31, 2007. For additional information concerning the Dime goodwill litigation and the LTWs, see the Company's Current Report on Form 8-K, dated March 12, 2003, File No. 1-14667.

In a series of decisions issued in 2002, the Court of Federal Claims granted the Company's summary judgment motions as to contract liability with respect to the four acquisitions involving financial assistance, but granted the U.S. Government's motions with respect to the four unassisted acquisitions. On September 29, 2003, the Court denied the U.S. Government's motion for summary judgment with respect to the claim for the Company's lost profits, but granted the U.S. Government's motion with respect to the Company's alternative claims for reliance damages and for the value of the lost supervisory goodwill. A six-week trial on the Company's lost profits claim started in June 2005, followed by a post-trial briefing which was completed in November 2005. The case now awaits a decision on damages from the trial judge. There can be no assurance or accurate prediction of the timing or the amount of damages that will be awarded by the trial judge. In addition, each of the trial

judge's decisions, including its findings on the U.S. Government's contract liability and any damages awarded, is subject to appeal.

Litigation is inherently uncertain, and significant uncertainty surrounds the legal issues involved in cases involving supervisory goodwill that underlie the value of the LTWs. The Company cannot accurately predict the timing or amount of any damages, whether the U.S. Government will decide to appeal any of the trial judge's decisions or the outcome of any appeals. As a result, the Company cannot predict if or when the conditions will be satisfied that will result in holders becoming entitled to exercise their LTWs or the value for which the LTWs will become exercisable.

#### **Comparison of 2006 to 2005**

The following discussion and analysis provides a comparison of the Company's results of operations between 2006 and 2005. Financial tables within the Earnings Performance from Continuing Operations supplement this discussion.

#### *Corporate Results of Operations*

##### **Net Interest Income**

For 2006, net interest income decreased \$97 million, or 1%, compared with 2005. The decrease was due to a 19 basis point decline in the net interest margin as an increase in the cost of interest-bearing liabilities, driven by higher short-term interest rates and a more competitive deposit pricing environment, outpaced the increase in the yield on interest-earning assets. Partially offsetting the decline in the net interest margin was a 6% increase in average interest-earning assets, driven primarily by an increase in home loans held in portfolio and growth in the credit card portfolio.

##### **Noninterest Income**

Noninterest income totaled \$6.38 billion in 2006, compared with \$5.10 billion in 2005. The increase is primarily due to the full year effect of consumer loan sales and servicing revenue and credit card fee income in 2006, which resulted from the Company's October 1, 2005 acquisition of Provident. Revenue from sales and servicing of consumer loans increased by \$1.11 billion and credit card fee income increased by \$498 million for the year ended December 31, 2006. The strong consumer response to the Company's new free checking product, which was launched early in 2006, also contributed to the growth in noninterest income, with depositor and other retail banking fees totaling \$2.57 billion in 2006, a 17% increase from the 2005 total of \$2.19 billion. Also contributing to the increase in noninterest income was a decrease in loss from sales of other available-for-sale securities primarily due to costs incurred with the partial restructuring of the securities portfolio in 2005, of which \$3 billion of lower-yielding debt securities were sold and subsequently replaced by the purchase of debt securities with comparatively higher yields. In addition, the Company received a \$149 million litigation award from the partial settlement of the Company's claims against the U.S. Government with regard to the Home Savings supervisory goodwill lawsuit in 2006. Partially offsetting these increases was a significant decline in revenue from the Company's home mortgage loan operations. Revenue from sales and servicing of home mortgage loans, including the effects of all MSR risk management instruments, was \$712 million, compared with \$1.78 billion in 2005. The decline was associated with the flat-to-inverted yield curve that existed throughout 2006, which resulted in a significant increase in MSR risk management costs, as compared with 2005. Additionally, a 24% year-over-year decline in home loan volume in 2006, reflecting the slowdown in the housing market, along with an industry-wide decline in subprime mortgage secondary market performance during the latter part of the year, led to lower gain on sale results. Insurance income decreased \$45 million due to lower reinsurance income and a decline in mortgage-related insurance income. Trading assets loss, excluding the revaluation gain or loss from

trading securities used to economically hedge the MSR, increased largely due to changes in the value of retained interests from mortgage loan securitizations.

### **Noninterest Expense**

Compensation and benefits expense increased \$236 million, or 6%, from 2005 primarily due to the addition of the Company's credit card operations, severance costs associated with the Company's productivity, efficiency and outsourcing initiatives and the addition of 85 net new retail banking stores in the last twelve months. The number of employees decreased from 60,798 employees at December 31, 2005 to 49,824 employees at December 31, 2006. Severance charges were approximately \$102 million for the year ended December 31, 2006 compared with \$17 million for the year ended December 31, 2005. The increase in occupancy and equipment expense during 2006 was primarily due to charges of approximately \$185 million related to the Company's productivity and efficiency initiatives, which included the consolidation of back-office support operations and other administrative functions. The increase in telecommunications and outsourced information services expense during 2006 was predominantly due to the addition of the Company's credit card operations. The increase in advertising and promotion expense during 2006 was predominantly due to marketing expenses incurred from the Company's credit card operations. A significant portion of the increase in professional fees during 2006 was due to charges from the early termination of technology contracts as a result of the Company's productivity and efficiency initiatives. Postage expense increased during 2006 largely due to increased direct mail solicitation volume related to the Company's credit card operations. The decrease in loan expense during 2006 was primarily due to a decrease in home loan volume resulting from the slowdown in the housing market. The increase in other expense from 2005 was partly due to transaction costs associated with the partial sale of the Company's MSR asset and an increase in amortization expense of intangible assets related to the Company's purchase of Provident in the fourth quarter of 2005.

#### *Operating Segment Results of Operations*

### **Retail Banking Group**

The increase in net interest income was predominantly due to rising short-term interest rates, which increased the funds transfer rate paid on retail deposits, partially offset by a decline in home loan net interest income. The increase in provision for loan losses was due to increased average balances on loans and changes in the product mix to home equity products. The increase in noninterest income was substantially due to a 17 percent growth in depositor and other retail banking fees reflecting higher levels of transaction fees and continued growth in the number of retail checking accounts. The increase in noninterest expense was largely due to higher compensation and benefits expense due to a decline in deferred compensation resulting from lower loan originations and higher occupancy and equipment expense due to expansion of the retail banking distribution network.

### **Card Services Group (Managed basis)**

During 2006, growth in the credit card franchise resulted in an increase in average loans to \$21.29 billion on a customer base of over 10 million accounts. During 2006, the Card Services Group opened approximately 3 million new accounts, with a significant part of this growth resulting from cross-selling credit card products to retail banking customers. Managed credit card receivables of \$23.50 billion at December 31, 2006 were up 18 percent from the end of 2005. The Card Services Group's credit performance benefited from a lower level of bankruptcy related charge-offs than occurred prior to the October 2005 change in consumer bankruptcy law, and from the sale of higher risk credit card accounts during the latter part of 2006. Managed net charge-offs at December 31, 2006 were 5.83 percent, down from 7.28 percent at December 31, 2005.



### **Commercial Group**

The decrease in net interest income was substantially due to higher transfer pricing charges, due to rising short-term interest rates combined with a shift from adjustable-rate to fixed-rate and hybrid loans, which more than offset increased interest income on a larger portfolio of multi-family loans. The negative \$82 million provision in 2006 was primarily the result of a \$60 million reduction in the allowance for loan losses that occurred as a result of two primary changes to the assumptions and methodologies used to estimate the allowance attributable to multi-family loans. First, as part of an ongoing program of model improvement, the Company introduced a new model that uses a formulaic, statistical-based approach to determine loss factors based on relevant default-predictive variables such as loan-to-value and debt service coverage ratios, and geographic factors. The second change was the adoption of a three year loss confirmation period for multi-family loans, replacing the four year estimate of the loss confirmation period. The negative provision in 2005 was the result of the runoff of higher risk commercial loans and growth in the portfolio of lower risk multi-family and commercial real estate loans. Noninterest income decreased primarily due to a \$59 million pretax gain on the sale of a real estate investment property and a \$55 million gain on the sale of mortgage-backed securities during 2005. The increase in noninterest expense during 2006 compared with 2005 reflects additional expenses related to the acquisition of Commercial Capital Bancorp and a reduction in contingent liability reserves incurred during 2005.

### **Home Loans Group**

The decrease in net interest income was primarily due to lower average balances of loans held for sale as a result of decreased loan volumes and lower spreads on loans. The increase in provision for loan losses during 2006 was primarily due to growth in the portfolio of purchased home equity loans and higher levels of delinquencies in the subprime mortgage channel. The decrease in noninterest income was substantially due to a less favorable MSR hedging environment in 2006 compared with 2005. Additionally, the gain from mortgage loans was lower due to the slowdown in the housing market and a decline in the secondary market performance of loans sold through the subprime mortgage channel. The decrease in noninterest expense was primarily due to a significant decline in employee headcount, as a result of the Company's efficiency initiatives.

### **Corporate Support/Treasury and Other**

The increase in net interest expense from 2005 to 2006 was due to increasing short-term interest rates which drove higher interest expense on FHLB borrowings, and a significant increase in the average balance of brokered certificates of deposit. The increase in noninterest income was primarily due to a litigation award of \$149 million from the partial settlement of the Home Savings supervisory goodwill lawsuit, a gain of \$74 million related to the transfer from held for investment to held for sale of \$17.79 billion of medium-term adjustable-rate home loans and the associated derivatives executed to hedge that transaction and a \$52 million increase in the cash surrender value of the Company's bank-owned life insurance. The increase in noninterest expense was predominantly due to charges of \$315 million associated with the Company's productivity and efficiency initiatives and a charge of \$67 million associated with the sale in 2006 of a significant portion of the Company's MSR. On December 31, 2006, the Company recognized a gain of \$415 million, net of tax, upon completion of the sale of WM Advisors, Inc.

### **Factors That May Affect Future Results**

The Company's Form 10-K and other documents that it files with the Securities and Exchange Commission contain forward-looking statements. In addition, the Company's senior management may make forward-looking statements orally to analysts, investors, the media and others. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts.

They often include words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates," or words of similar meaning, or future or conditional verbs such as "will," "would," "should," "could" or "may."

Forward-looking statements provide management's current expectations or predictions of future conditions, events or results. They may include projections of the Company's revenues, income, earnings per share, capital expenditures, dividends, capital structure or other financial items, descriptions of management's plans or objectives for future operations, products or services, or descriptions of assumptions underlying or relating to the foregoing. They are not guarantees of future performance. By their nature, forward-looking statements are subject to risks and uncertainties. These statements speak only as of the date made and management does not undertake to update them to reflect changes or events that occur after that date except as required by federal securities laws.

There are a number of significant factors which could cause actual conditions, events or results to differ materially from those described in the forward-looking statements, many of which are beyond management's control or its ability to accurately forecast or predict. Factors that might cause our future performance to vary from that described in our forward-looking statements include market, credit, operational, regulatory, strategic, liquidity, capital and economic factors as discussed in "Management's Discussion and Analysis" and in other periodic reports filed with the SEC. In addition, other factors besides those listed below or discussed in reports filed with the SEC could adversely affect our results and this list is not a complete set of all potential risks or uncertainties. Significant among the factors are the following:

*Economic conditions that negatively affect housing prices and the job market have resulted, and may continue to result, in a deterioration in credit quality of the Company's loan portfolios, and such deterioration in credit quality has had, and could continue to have, a negative impact on the Company's business.*

Washington Mutual is one of the nation's largest lenders, and deterioration in the credit quality of the Company's loan portfolios can have a negative impact on earnings resulting from increased provisioning for loan losses and from increased nonaccrual loans, which could cause a decrease in interest-earning assets. Credit risk incorporates the risk of loss due to adverse changes in a borrower's ability to meet its financial obligations on agreed upon terms. The overall credit quality of the Company's loan portfolios is particularly impacted by the strength of the U.S. economy and local economies in which the Company conducts its lending operations as well as trends in residential housing prices. The Company continually monitors changes in the economy, particularly unemployment rates and housing prices, because these factors can impact the ability of the Company's borrowers to repay their loans.

During 2007, the housing market in the United States (particularly in California and Florida, where properties securing approximately 48% and 10% of the Company's outstanding single-family residential mortgage loans are located) began to experience significant adverse trends, including accelerating price depreciation in some markets and rising delinquency and default rates. These conditions led to significant increases in loan delinquencies and credit losses in the Company's mortgage portfolios and higher provisioning for loan losses which has adversely affected the Company's earnings. The Company expects that housing prices will experience significant further deterioration in 2008 with further adverse effects on its operating results, business and financial condition. Furthermore, the Company expects that the onset of a recession either in the United States as a whole or in specific regions of the country, or the occurrence of a major natural or other disaster in the United States, would significantly increase the level of delinquencies and credit losses. Increases in credit costs would reduce the Company's earnings and adversely affect its capital position and financial condition.

The Company makes various assumptions and judgments about the collectibility of its loan portfolios when estimating the allowance for loan losses, which represents management's estimate of incurred credit losses inherent in the loan portfolio as of the balance sheet date. The estimate of the

allowance is based on a variety of factors, including past loan loss experience, the current credit profile of borrowers, adverse situations that have occurred that may affect a borrower's ability to meet his financial obligations, the estimated value of underlying collateral, general economic conditions, and the impact that changes in interest rates and employment conditions have on a borrower's ability to repay adjustable-rate loans. Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. The Company collects information on the performance of loans in its portfolios and routinely uses this information to recalibrate the formulaic models used in estimating the allowance for loan losses. Subsequent evaluations of the loan portfolio may reveal that estimated levels of loss severity used in estimating the allowance for loan losses differed significantly from actual experience, and in such circumstances the Company may have to record an increased provision for loan losses in subsequent periods thereby reducing earnings in those periods.

Until recently, the Company originated and purchased from third-party lenders loans to higher risk borrowers through its subprime mortgage channel. Borrowers in the subprime mortgage channel tend to have greater vulnerability to changes in economic and housing market factors, such as increases in unemployment, a slowdown in housing price appreciation or declines in housing prices, than do other borrowers. Additionally, the tightening of underwriting standards throughout the mortgage industry have significantly reduced the eligibility of borrowers to obtain credit, or to find credit on affordable terms. The performance of this loan portfolio in recent quarters has been, and in the future will likely continue to be, negatively impacted by a variety of factors, including changes in the economic factors noted above, which negatively impact borrowers.

*The Company's access to market-based liquidity sources may be negatively impacted if market conditions persist or if further ratings downgrades occur. Funding costs may increase from current levels, and gain on sale may be reduced, leading to reduced earnings.*

While the Company actively manages its liquidity risk and maintains liquidity at least sufficient to cover all maturing debt obligations or other forecasted funding requirements over the next twelve months (see "Liquidity Risk and Capital Management"), the Company's liquidity may be affected by an inability to access the capital markets or by unforeseen demands on cash. This situation may arise due to circumstances beyond the Company's control, and is subject to the Company's and its subsidiaries' credit ratings as assigned by various nationally recognized statistical rating organizations ("NRSROs"). During 2007, disruptions in the capital markets substantially limited the ability of mortgage originators, including Washington Mutual, to sell mortgage loans to the capital markets through whole loan sales or securitization. As a result, the Company experienced a general loss of liquidity in most secondary markets for both its loan and asset-backed securities holdings, and this condition has persisted to the present time. The Company cannot forecast if or when either specific secondary markets or broader market liquidity conditions will see improvement from current stresses, although it is the Company's expectation that the existing turmoil in secondary loan and asset-backed securities markets may continue to affect its performance, described below, throughout 2008.

As a result of these conditions, secondary loan sales are currently limited primarily to sales of conforming loans to government-sponsored enterprises ("GSEs"), and the Company cannot predict when secondary markets for nonconforming loans, credit card receivables, and other loan assets will reopen. As such, the Company has in recent periods retained for its own account substantially all of the loans and receivables the Company has originated or purchased, other than conforming mortgage loans. The Company will generally be unable to recognize gains on sale, and may be required to establish reserves for loans that remain on its balance sheet, which may reduce earnings. In addition, the Company has taken steps to reduce or eliminate its origination of assets for which limited secondary market liquidity exists.

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While the Company remains comfortable with its ability to fund mortgage loans (see "Liquidity Risk and Capital Management"), the Company's ability to sell conforming loans is dependent on its relationships with the GSEs. The Company presently sells a substantial portion of its conforming residential originations to the GSEs, primarily Freddie Mac. The ability of the GSEs to continue to purchase loans at current volume levels is dependent in part on their own capital positions and the levels of defaults in the portfolios underlying the mortgage-backed securities issued by the GSEs. The Company's liquidity and earnings could be adversely affected if the GSEs were unwilling to purchase the Company's residential loan products.

The Company has generally securitized a large portion of its credit card portfolio, which provided additional liquidity for the Company. Due to disruptions in the secondary market for credit card receivables, the Company is presently not able to securitize credit card receivables on terms it considers acceptable. As a result, the Company's liquidity will be adversely affected until the credit card securitization market normalizes. Additionally, the Company will be required to provide additional loss reserves for the credit card receivables that it retains in its portfolio, which will adversely affect earnings.

Current market conditions have also limited the Company's liquidity sources to secured funding outlets such as the Federal Home Loan Banks and repurchase agreements, and to FDIC-insured deposits originated through either brokers or through its branch network. Other sources of funding, such as medium-term notes, uninsured institutional deposits, and certain escrow balances have largely been closed to the Company. Many of these sources are ratings-sensitive, and due to recent negative ratings actions, the Company does not expect these sources to return as reliable sources of funding even if general market liquidity conditions improve until the Company's ratings improve. For example, institutional depositors generally require issuers to have the highest short-term ratings from at least one of the major rating agencies; however, as a result of recent actions, the Company and its banking subsidiaries are now generally in the second-highest short-term rating category.

The Company's rating profile remains "investment grade" as defined by NRSROs. No assurance can be given, however, that the Company will be able to retain an "investment grade" rating. The loss of investment grade ratings would likely result in further reductions in the sources of liquidity available to the Company; may result in increased collateral or margining requirements under derivative and repurchase agreements with counterparties, which could increase the Company's funding costs and further reduce its earnings and liquidity; and could adversely affect the Company's ability to conduct its normal business operations, in ways that could be material.

The Company's liquidity could also be adversely affected by unanticipated demands on its cash, such as having to repurchase securitized loans if it were found to have violated representations and warranties contained in the securitization agreements. In such event, the Company generally would be required to repurchase these loans or indemnify the investor for losses sustained. Since in most instances the repurchased loans would be in default, it is unlikely that the Company would be able to resell these loans in the secondary market. If the Company were required to repurchase a substantial amount of these loans, its liquidity and capital would be adversely affected as the amount of nonperforming assets on its balance sheet would increase.

*If the Company has significant additional losses, it may need to raise additional capital, which could have a dilutive effect on existing shareholders, and it may affect its ability to pay dividends on its common and preferred stock.*

The Company's primary subsidiary, Washington Mutual Bank, must maintain certain minimum capital ratios in order to remain a "well-capitalized" institution for regulatory purposes. While the Company believes it has sufficient capital for its operations (see "Liquidity Risk and Capital Management"), if the Bank is unable to meet its minimum capital ratios, the Company or the Bank would be forced to raise additional capital. No assurance can be given that sufficient additional capital

would be available nor as to the terms on which capital would be available. If sufficient capital were not available, the Company would consider a variety of alternatives, including the sale of assets. Under such forced sale conditions, the Company may not be able to realize fair value for the assets sold. Other alternatives would include changing the Company's business practices or entering into equity transactions. Even if capital is available, the terms and pricing of such securities could be dilutive to existing shareholders and cause the price of the Company's outstanding securities to decline.

The Company depends on dividends, distributions and other payments from its banking and nonbanking subsidiaries to fund dividend payments on common and preferred stock and to fund all payments on its other obligations, including debt obligations. If the earnings of the Company's subsidiaries are not sufficient to make dividend payments to the Company while maintaining adequate capital levels, the Company may not be able to make dividend payments to its common or preferred shareholders.

*Changes in interest rates may adversely affect the Company's business, including net interest income and earnings.*

Like other financial institutions, Washington Mutual and its banking subsidiaries raise funds for the Company's business by, among other things, borrowing money in the capital markets and from the Federal Home Loan Bank system and accepting deposits from depositors, which the Company uses to make loans to customers and invest in debt securities and other interest-earning assets. The Company earns interest on these loans and assets and pays interest on the money it borrows and on the deposits it accepts from depositors. Changes in interest rates, including changes in the relationship between short-term rates and long-term rates, may have negative effects on the Company's net interest income and therefore its earnings. Changes in interest rates and responses by the Company's competitors to those changes may affect the rate of customer prepayments for mortgages and other term loans and may affect the balances customers carry on their credit cards. These changes can reduce the overall yield on the Company's assets. Changes in interest rates and responses by the Company's competitors to these changes may also affect customer decisions to maintain balances in the deposit accounts they have with the Company. These changes may require us to replace withdrawn balances with higher-cost alternative sources of funding.

In addition, changes in interest rates may affect the Company's mortgage banking business in complex and significant ways. For example, changes in interest rates can affect gain from mortgage loans and loan servicing fees, which are the principal components of revenue from sales and servicing of home mortgage loans. When mortgage rates decline, the fair value of the mortgage servicing rights ("MSR") asset generally declines and gain from mortgage loans tends to increase, to the extent the Company is able to sell or securitize mortgage loans in the secondary market. When mortgage rates rise, the Company generally expects loan volumes and payoffs in its servicing portfolio to decrease. As a result, the fair value of its MSR asset generally increases and gain from mortgage loans decreases. In recent periods, however, declines in general interest rates have resulted in slower increases in prepayment rates than in prior periods of declining interest rates, due in part to the reduced liquidity and tightened underwriting standards in the mortgage market making refinancing by borrowers more difficult.

As part of the Company's overall risk management activities, the Company seeks to mitigate changes in the fair value of its MSR asset by purchasing and selling financial instruments, entering into interest rate contracts and forward commitments to purchase or sell mortgage-backed securities and adjusting the mix and amount of such financial instruments or contracts to take into account the effects of different interest rate environments. The MSR asset and the mix of financial instruments used to mitigate changes in its fair value are not perfectly correlated. This imperfect correlation creates the potential for excess MSR risk management gains or losses during any period. Management must exercise judgment in selecting the amount, type and mix of financial instruments and contracts to

mitigate changes in the fair value of the Company's MSR. The Company cannot assure that the amount, type and mix of financial instruments and contracts it selects will fully offset significant changes in the fair value of the MSR, and the Company's actions could negatively impact its earnings. The Company's reliance on these risk management instruments may be impacted by periods of illiquidity in the secondary markets, which could negatively impact the performance of the MSR risk management instruments. For further discussion of how interest rate risk, basis risk, volatility risk and prepayment risk are managed, see "Market Risk Management."

*Certain of the Company's loan products have features that may result in increased credit risk.*

The Company has significant portfolios of home equity loans, which are secured by a first or second lien on the borrower's property. When the Company holds a second lien on a property which is subordinate to a first lien mortgage held by another lender, both the probability of default and severity of loss risk is generally higher than when the Company holds both the first and second lien positions. Home equity loans and lines of credit with combined loan-to-value ratios of greater than 80 percent also expose the Company to greater credit risk than home loans with loan-to-value ratios of 80 percent or less at origination. This greater credit risk arises because, in general, both default risk and the severity of loss risk are higher when borrowers have less equity in their homes.

The Company originates Option ARM loans under which borrowers have the option of making minimum payments based on an interest rate that is lower than the fully-indexed rate. Borrowers who continue to make minimum payments will generally experience negative amortization as unpaid interest is capitalized and added to the principal amount of the loan. The minimum payment resets to a fully-amortizing payment at the earlier of five years from origination or when the amount of negative amortization reaches specified levels. The risk that Option ARM borrowers will be unable to make increased loan payments as a result of the minimum payment on the loan adjusting upward to a fully-amortizing payment is a key risk associated with the Option ARM product.

The Company originates interest-only loans that it either securitizes or holds in its portfolio. Borrowers with interest-only loans are initially required to make payments that are sufficient to cover accrued interest. After a predetermined period (generally five years), the payments are reset to allow the loan to fully amortize over its remaining life. Borrowers with interest-only loans are particularly affected by declining housing prices because there is no amortization of principal on the loans. Such economic trends could cause the credit performance of interest-only loans to deteriorate more rapidly than other types of loans with a negative impact on the Company's results. For further discussion of credit risk, see "Credit Risk Management."

Consistent with mortgage industry underwriting practices, loans underwritten with limited documentation of income, net worth or credit history are widely represented within the Company's single-family residential loan products. In particular, such practices are frequently applied to the origination of Option ARM products. Accordingly, approximately 75% of the Company's Option ARM portfolio was originated using a limited documentation standard. As limited documentation loans have a higher risk of default than loans with full documentation, a continued downturn in economic conditions or a further decrease in housing prices could result in higher default rates in the Company's loan portfolio.

*The Company uses estimates in determining the fair value of certain of our assets, which estimates may prove to be imprecise and result in significant changes in valuation.*

A portion of the Company's assets are carried on the balance sheet at fair value, including: the Company's trading assets including certain retained interests from securitization activities, available-for-sale securities, derivatives and MSR. Generally, for assets that are reported at fair value, the Company uses quoted market prices or internal valuation models that utilize observable market data inputs to estimate their fair value. In certain cases, observable market prices and data may not be

readily available or their availability may be diminished due to market conditions. The Company uses financial models to value certain of these assets. These models are complex and use asset specific collateral data and market inputs for interest rates. Although the Company has processes and procedures in place governing internal valuation models and their testing and calibration, the Company cannot assure that it can properly manage the complexity of its models and valuations to ensure, among other things, that the models are properly calibrated, the assumptions are reasonable, the mathematical relationships used in the model are predictive and remain so over time, and the data and structure of the assets and hedges being modeled are properly input. Such assumptions are complex as the Company must make judgments about the effect of matters that are inherently uncertain. Different assumptions could result in significant changes in valuation, which in turn could affect earnings or result in significant changes in the dollar amount of assets reported on the balance sheet.

*The Company is subject to risks related to credit card operations, and this may adversely affect its credit card portfolio and its ability to continue growing the credit card business.*

Credit card lending brings with it certain risks and uncertainties. These include the composition and risk profile of the Company's credit card portfolio and the Company's ability to continue growing the credit card business. Credit cards typically have smaller balances, shorter lifecycles and experience higher delinquency and charge-off rates than real estate secured loans. Delinquencies and credit losses in the consumer finance industry generally increase during economic downturns or recessions. Likewise, consumer demand may decline during an economic downturn or recession. Account management efforts, seasoning and economic conditions, including unemployment rates and housing prices, affect the overall credit quality of the Company's credit card portfolio. The success of the credit card business also depends, in part, on the success of the Company's product development, product rollout efforts and marketing initiatives, including the rollout of credit card products to the Company's existing retail and mortgage loan customers, and the Company's ability to continue to successfully target creditworthy customers.

Recent disputes involving the Visa and MasterCard networks, including their membership standards and pricing structures, could also result in changes that would be adverse to the credit card business. Changes in interest rates can also negatively affect the credit card business, including costs associated with funding the credit card portfolio, as described above under "Changes in interest rates may adversely affect the Company's business, including net interest income and earnings."

*The Company is subject to operational risk, which may result in incurring financial and reputational losses.*

The Company is exposed to many types of operational risk, including the risk of fraud by employees or outsiders, the risk of operational errors, including clerical or record-keeping errors or those resulting from faulty or disabled computer or telecommunications systems. Given the Company's high volume of transactions, certain errors may be repeated or compounded before they are discovered and successfully corrected. The Company's dependence upon automated systems to record and process transactions may further increase the risk that technical system flaws or employee tampering with or manipulation of those systems will result in losses that are difficult to detect.

The Company may be subject to disruptions of its systems, arising from events that are wholly or partially beyond the Company's control (including, for example, computer viruses or electrical or telecommunications outages), which may give rise to losses in service to customers and to financial loss or liability. The Company is further exposed to the risk that its external vendors may be unable to fulfill their contractual obligations (or will be subject to the same risk of fraud or operational errors by their respective employees as we are) and to the risk that the Company's (or the Company's vendors') business continuity and data security systems prove to be inadequate. The Company relies on offshoring of services to vendors in foreign countries for certain functions and this creates the risk of incurring losses arising from unfavorable political, economic and legal developments in those countries.

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The Company also faces the risk that the design of its controls and procedures may prove to be inadequate or are circumvented, thereby causing delays in detection of errors or inaccuracies in data and information. Although the Company maintains a system of controls designed to keep operational risk at appropriate levels, it is possible that any lapses in the effective operations of controls and procedures could materially affect earnings or harm the Company's reputation. In an organization as large and complex as Washington Mutual, lapses or deficiencies in internal control over financial reporting could be material to the Company.

In addition, the Company is heavily dependent on the strength and capability of its technology systems which it uses both to interface with its customers and to manage internal financial and other systems. The Company's ability to run its business in compliance with applicable laws and regulations is dependent on these infrastructures.

The Company depends on the expertise of key personnel and faces competition for talent. The Company's success depends, in large part, on its ability to hire and retain key people. If the Company is unable to retain these people and to attract talented people, or if key people fail to perform properly, the Company's business may suffer. For further discussion of operational risks, see "Operational Risk Management."

*The Company's failure to comply with laws and regulations could have adverse effects on the Company's operations and profitability.*

The Company operates in a regulated industry and is subject to a wide array of laws and regulations that apply to almost every element of its business, including banking, mortgage, securities, consumer lending and deposit laws and regulations. Failure to comply with these laws and regulations could result in financial and operational penalties, including fines, restrictions on otherwise permissible activities and receivership. In addition, establishing systems and processes to achieve compliance with these laws and regulations may increase its costs and/or limit its ability to pursue certain business opportunities.

Effective October 17, 2007, Washington Mutual Bank consented to the issuance by the Office of Thrift Supervision ("OTS") of a cease and desist order requiring Washington Mutual Bank to comply with the Bank Secrecy Act ("BSA") and related BSA regulations and regulations governing suspicious activity reporting. Although no fines or restrictions on Washington Mutual Bank's activities have been imposed by the OTS, failure by the Company to comply with the terms of this order or other applicable laws and regulations could have a material adverse effect on the Company's business, financial condition or operating results through the imposition of additional sanctions.

The volume of claims and amount of damages and penalties claimed in litigation and regulatory proceedings against financial institutions remain high. Substantial legal liability or significant regulatory action against the Company and its subsidiaries could adversely affect the Company's financial results or cause reputational harm to the Company, which in turn could seriously harm its business prospects. For further discussion of pending legal actions that may affect the Company, see "Legal Proceedings."

*Changes in the regulation of financial services companies, housing government-sponsored enterprises and credit card lenders could adversely affect the Company.*

The banking and financial services industries, in general, are heavily regulated. Proposals for legislation further regulating the banking and financial services industry are continually being introduced in the United States Congress and in state legislatures. The agencies regulating the financial services industry also periodically adopt changes to their regulations.

Proposals that are now receiving a great deal of attention and could significantly impact the Company's business include changes to consumer protection initiatives relating to bank overdraft practices, security of customer information, marketing practices, nontraditional mortgage loan products



including Option ARM loans and interest-only products, credit card lending practices, fees charged to merchants for credit and debit card transactions and mortgage lending and servicing practices. For instance, the Federal Reserve Board has proposed amendments to Regulation Z, which implements the Truth in Lending Act and the Home Ownership Equity Protection Act, to require new disclosures and restrict certain lending practices with regard to mortgage lending. The Federal Reserve Board has also proposed amendments to Regulation Z that would require changes to the format, timing, and content of credit card disclosures. Legislation calling for increased regulation of mortgage and credit card lending is also receiving serious consideration in Congress and in the state legislatures. In 2007, the U.S. House of Representatives passed legislation that would impose new responsibilities on mortgage lenders and restrict certain mortgage lending and servicing practices.

Policymakers are also considering a number of initiatives to assist borrowers who are having difficulty repaying their home loans. On December 5, 2007, President Bush proposed a plan for a five year moratorium on interest rate resets for certain subprime mortgages held by qualifying borrowers. Other public officials and private groups have proposed similar plans. The U.S. House of Representatives Judiciary Committee has reported out legislation that would allow judges to modify the terms of certain mortgages in Chapter 13 bankruptcies. On February 13, 2008, President Bush signed the Economic Stimulus Act of 2008 into law. Among other things, the legislation will raise the Federal Housing Administration ("FHA") loan limit to 125 percent of the area median house price (as determined by the Secretary of Housing and Urban Development) up to a maximum of \$729,750 for loans approved by December 31, 2008, and will increase the Fannie Mae and Freddie Mac conforming loan limit to the same amount for loans originated between July 1, 2007 through December 31, 2008.

In addition, there continues to be a focus on reform of the regulatory oversight of the housing government-sponsored enterprises including the Federal Home Loan Bank system. The Company is unable to predict whether any of these proposals will be implemented or in what form and what effect any such proposal could have on its business or operating results.

It is possible that one or more legislative proposals may be adopted or regulatory changes may be made that would have an adverse effect on the Company's business. For further discussion of the regulation of financial services, see "Regulation and Supervision" and Note 20 to the Consolidated Financial Statements "Regulatory Capital Requirements and Dividend Restrictions."

*The Company's business and earnings are highly sensitive to general business, economic and market conditions, and continued deterioration in these conditions may adversely affect its business and earnings.*

The Company's business and earnings are highly sensitive to general business and economic conditions. These conditions include the strength of the U.S. economy and the local economies in which the Company conducts business, in particular the strength of national and local job markets, the level of interest rates, the slope of the yield curve, the level of inflation, the value of the U.S. dollar as compared to foreign currencies and fluctuations in the level or the volatility in debt, equity and housing markets. Changes in these conditions may adversely affect the Company's business and earnings. For example, when short-term interest rates rise, there is a lag period until adjustable-rate mortgages reprice. As a result, the Company may experience compression of its net interest margin with a commensurate adverse effect on earnings. Likewise, the Company's earnings could also be adversely affected when a flat or inverted yield curve develops, as this may inhibit its ability to grow its adjustable-rate mortgage portfolio and may also cause margin compression. A prolonged economic downturn could increase the number of customers who become delinquent or default on their loans. A rising interest rate environment could increase the negative amortization of Option ARM loans, which may eventually result in increased delinquencies and defaults. Rising interest rates could also decrease customer demand for loans.

The Company's business and earnings are significantly affected by the fiscal and monetary policies of the federal government and its agencies. The Company is particularly affected by the policies of the

Federal Reserve Board, which regulates the supply of money and credit in the United States. Federal Reserve policies directly and indirectly influence the yield on the Company's interest-earning assets and the cost of its interest-bearing liabilities. Changes in those policies are beyond the Company's control and are difficult to predict.

*The Company may face damage to its professional reputation and business as a result of allegations and negative public opinion as well as pending and threatened litigation.*

Reputational risk, meaning the risk to earnings and capital from negative public opinion, is inherent in Washington Mutual's business. Negative public opinion can result from the actual or perceived manner in which the Company conducts its business activities, which include its sales and trading practices, its loan origination and servicing activities, its retail banking and credit card operations, its management of actual or potential conflicts of interest and ethical issues and its protection of confidential customer information. Negative public opinion can adversely affect the Company's ability to keep and attract customers. The Company cannot assure that it will be successful in avoiding damage to its business from reputational risk.

*The Company is subject to significant competition from banking and nonbanking companies.*

The Company operates in a highly competitive environment and expects competition to continue as financial services companies combine to produce larger companies that are able to offer a wide array of financial products and services at competitive prices with attractive terms. In addition, customer convenience and service capabilities, such as product lines offered and the accessibility of services, are significant competitive factors.

The Company's most direct competition for loans comes from commercial banks, other savings institutions, investment banking firms, national mortgage companies and other credit card lenders. The Company's most direct competition for deposits comes from commercial banks, other savings institutions and credit unions doing business in the Company's markets. As with all banking organizations, the Company also experiences competition from nonbanking sources, including mutual funds, corporate and government debt securities and other investment alternatives offered within and outside of the Company's primary markets. In addition, technological advances and the growth of e-commerce have made it possible for non-depository institutions to offer products and services that were traditionally offered only by banks. Many of these competitors have fewer regulatory constraints and some have lower cost structures.

In addition, the Company competes on the basis of transaction execution, innovation and technology. The Company's industry is subject to rapid and significant technological changes. In order to compete in the Company's industry, Washington Mutual must continue to invest in technologies across all of its businesses, including transaction processing, data management, customer interactions and communications and risk management and compliance systems. The Company expects that new technologies will continue to emerge, and these new services and technologies could be superior to or render the Company's technologies obsolete. The Company's future success will depend in part on its ability to continue to develop and adapt to technological changes and evolving industry standards. If the Company is not able to invest successfully in and compete at the leading edge of technological advances across all of its businesses, its revenues and profitability could suffer.

*Each of the factors discussed in the preceding paragraphs can significantly impact the Company's businesses, operations, activities, condition and results in significant ways that are not described in the foregoing discussion and which are beyond the Company's ability to anticipate or control, and could cause actual results to differ materially from the outcomes described in the forward-looking statements.*

**PART III**

**EXECUTIVE COMPENSATION**

**Human Resources Committee Processes and Procedures**

**Overview**

Our Human Resources Committee is comprised of five non-employee directors, each of whom has been determined by our Board to be independent under NYSE rules. Members are nominated by the Governance Committee and approved by the Board. The current members of the Committee are:

James H. Stever, Chair  
Stephen E. Frank  
Charles M. Lillis  
Phillip D. Matthews  
Margaret Osmer McQuade

**How the Human Resources Committee Operates**

The Human Resources Committee operates under a written charter that specifies that the Committee is responsible for the general oversight of our compensation policies and practices, including those that relate to the executive officers listed in the Summary Compensation Table at page 103 of this Proxy Statement. In this Proxy Statement we refer to those executives as our "named executives." The Committee reviews its charter annually and may recommend changes it considers appropriate to the full Board. The Committee also conducts an annual self-evaluation to assess its performance for the year. The Committee has regularly scheduled meetings in January, February, July, October and December, and has special meetings whenever necessary to fulfill its responsibilities. In 2007, the Committee met six times. It also may act by unanimous written consent. With respect to some matters, it may delegate limited authority to one or more Company officers, although it does not delegate to officers the authority to determine the form or amount of an executive officer's compensation. The members meet in executive session at each meeting to discuss a variety of matters. The Committee also meets with various members of management, outside counsel and outside consultants to gain additional insight and perspective with respect to such matters as management succession, the CEO evaluation, legal matters, pension plan performance and compensation and benefits issues generally.

**The Human Resources Committee's Responsibilities**

The Human Resources Committee assists the Board in fulfilling the following responsibilities:

Establishing, developing and administering our executive officer compensation programs and long-term incentive plans;

Overseeing and administering our benefit plans;

Annually evaluating our CEO's performance and setting his compensation amounts accordingly with input from the full Board;

Reviewing and coordinating the approval of the CEO's goals; and

Reviewing the CEO's succession planning.

Specifically, the Human Resources Committee is responsible for annually reviewing and approving the base salary, the target annual bonus and any long-term incentive awards for the CEO and the other named executives. In this regard, the Committee approves the performance measures to be used in

executive, management and broad-based employee incentive plans and the levels of performance for which we will pay incentive compensation.

With respect to the compensation of our CEO, the Human Resources Committee annually approves financial and leadership goals and objectives relevant to the CEO's compensation and evaluates the CEO's performance in light of those goals. The Committee determines amounts and forms of the CEO's compensation, reports this information to the full Board, and considers whether adjustments to the CEO's compensation are appropriate based on input from the full Board.

The Human Resources Committee is also responsible for approving the base salary, annual target bonus and any long-term incentive awards for all officers subject to Section 16 of the Securities Exchange Act of 1934, which includes our senior executives with a corporate title of Executive Vice President, and certain of our executives with a corporate title of Senior Vice President. In doing so, the Committee considers the CEO's recommendations with respect to each of these executives and sets the compensation for each executive based on its evaluation of the executive's performance and its consideration of benchmarking data and internal pay equity. In addition, the Human Resources Committee meets annually to review our Company performance and individual executive performance for purposes of determining the annual incentive bonus paid to named executives and other officers by certifying the results under our Leadership Bonus Plan.

The Human Resources Committee is also responsible for establishing base salary, target annual bonus and long-term incentive awards for newly-hired executives and other senior officers who will be subject to Section 16 of the Securities Exchange Act of 1934 in their roles with our Company. To facilitate negotiations with talented executive candidates, the Committee has approved a standard offer letter and guidelines for base salary, target annual bonus and long-term incentive awards for newly-hired executives who will be members of our Executive Committee, and has delegated authority to the Committee's Chair to approve employment offer letters that fall within the guidelines. Offers that do not fall within the guidelines must be approved by the full Committee.

The Human Resources Committee is authorized to directly engage its own outside consultants, and for 2007 the Human Resources Committee directly retained Towers Perrin to: (i) assist in gathering benchmarking data and monitoring compensation trends in our industry and among large public companies generally, (ii) advise the Committee regarding compensation best practices and trends, and (iii) assist in the design and development of our executive compensation program. The Committee meets in executive session annually to review the performance of the outside compensation consultant, assess the firm's objectivity on executive compensation matters in light of other services our management engages the firm to perform, and generally assess the quality of the services Towers Perrin provides. Based on this assessment, the Committee decides whether to retain the outside compensation consultant for the upcoming year, or to conduct a search for a new compensation consultant.

While Towers Perrin has been engaged by, and directly reports to the Committee, the Committee has authorized Towers Perrin to work with management on behalf of the Committee, as necessary. There are a number of reasons for this interaction with Company management. Before regularly scheduled Human Resources Committee meetings, Towers Perrin meets with management to review relevant materials that will be presented to and discussed by the Committee and, when relevant, any proposals on which management will ask the Committee to act. At other times, Towers Perrin may contact management to obtain or confirm information that is necessary for the consultant to effectively advise the Committee on a variety of ad-hoc requests and inquiries made by the Committee. The parameters for this interaction were established when the Committee originally retained Towers Perrin as its advisor. In addition to services performed at the direction of the Committee, Towers Perrin also performs services at the direction of our management under separate engagements. In 2007 this work included actuarial services related to the WaMu Pension Plan and consulting services related to our health and welfare plans.

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In February 2008 the Committee adopted a policy requiring the Committee's pre-approval of Company engagements of the Committee's outside compensation consulting firm to perform services other than at the direction of the Committee. In pre-approving such other services, the Committee will consider, among other factors, whether the proposed services would affect the compensation consultant's ability to give impartial recommendations or advice to the Committee with regards to the Committee's work.

Our CEO provides recommendations to the Human Resources Committee regarding named executives' compensation (including base salary, target bonus and long-term incentive awards) and is responsible for conducting the performance evaluations for them. Our Chief Human Resources Officer, and members of his department, also support the Human Resources Committee and provide recommendations regarding the amount and form of compensation paid to executive officers.

The Human Resources Committee also administers our Amended and Restated 2003 Equity Incentive Plan, and has delegated the authority to the Chief Human Resources Officer to grant a limited number of stock options, restricted stock and performance shares under that plan to senior officers who are not executive officers.

## Compensation Discussion and Analysis

### Introduction

The Human Resources Committee of the Board of Directors, referred to as the Committee in this discussion, oversees and regularly reviews compensation programs for our executive officers, including the named executive officers listed in the Summary Compensation Table at page 103. The Committee sets annual compensation elements for the CEO, and approves annual compensation elements for other executive officers. Where we use the term "named executives" in this Compensation Discussion and Analysis we are referring to the named executive officers. Compensation for our named executives includes annual cash compensation (base salary and annual incentives), long-term incentives in the form of equity compensation, and qualified and non-qualified retirement programs. Company-paid perquisites were eliminated for named executives beginning in 2007. In addition, each executive has either a change-in-control agreement or an employment agreement that provides for payment in the event of termination under certain circumstances following a change-in-control of the Company, and severance benefits are provided for termination under certain other circumstances.

In setting compensation, the Committee considers its compensation objectives, competitive practices of our peers (outlined below), internal pay equity and the roles and responsibilities of each executive. The Committee sets compensation also to align with our current and long-term business strategy and goals. There is no formal weighting of any of these factors; the Committee uses its discretion in setting pay targets and amounts. The Committee reviews and discusses annual pay elements (base salary, bonus targets and equity awards) each year. It evaluates other programs as needed based on changes in compensation objectives, alignment with overall Company direction and business strategy, competitive trends and changes in tax law. Based upon a review of these factors, we have designed our executive compensation programs and have paid total compensation amounts to properly motivate named executives to execute our strategy, achieve our business goals and create shareholder value.

We paid significantly lower compensation to named executives in 2007 than in 2006, reflecting our objective and philosophy of paying for performance. Our emphasis on at-risk performance-based compensation resulted in significantly lower 2007 annual incentive bonus payouts and restricted stock vesting, no payout for the 2005-2007 performance share cycle, and zero in-the-money value of prior stock option grants at December 31, 2007 since our closing stock price on that date was below the exercise price of every outstanding stock option held by named executives. These effects are the direct result of disappointing Company financial results due primarily to the extreme turmoil in the mortgage and credit markets.

For 2008 we have structured our long-term equity incentive and annual incentive bonus programs for named executives to align with our objective to improve Company performance in 2008 and beyond. We continue to provide at least 50% of total direct compensation to executives (over 70% for the CEO) in the form of long-term equity incentive compensation which is directly linked to stock price and total shareholder return. Our 2008 long-term equity incentive compensation awards provide strong incentives to named executives to restore shareholder value through increased stock price by tying stock option vesting to the price of our common stock achieving certain thresholds. Our 2008 annual incentive bonus plan is designed to align executive bonus compensation with the achievement of four objective performance measures that are core to the success of our business: (i) net operating profit, (ii) noninterest expense, (iii) depositor and other retail banking fees, and (iv) customer loyalty. In addition to these objective measures, when determining appropriate bonus payouts after the end of 2008 the Committee will evaluate the Company's performance in credit risk management and overall corporate profitability in light of actual events and market conditions during the year.

**Objectives of Our Compensation Programs**

We design our executive compensation programs to achieve the following objectives:

Our compensation programs should enable us to attract and retain the key executive talent we need on a long-term basis to manage our business.

The substantial majority of each executive's annual compensation should be performance-based such that executives realize value only if we achieve our business goals and objectives and create shareholder value.

Performance targets for incentive compensation should align with our annual and long-term business strategy.

Total compensation amounts should balance the need to be competitive with our industry peers while also being consistent with the key business objective of controlling costs.

Total compensation amounts among named executives should be consistent with our philosophy of internal pay equity by appropriately reflecting the role, scope and complexity of each executive's position relative to other executives.

**Elements of Executive Compensation**

As shown in the table below, our 2007 executive compensation program incorporated a number of diverse elements designed to achieve our compensation objectives in a variety of ways.

<b>Short-term Elements</b>	<b>How Objectives Are Met</b>
Base Salary	Provides an annually fixed level of pay that reflects the role, scope and complexity of each executive's position relative to other executives.
Cash Bonus	Performance-based compensation payable only upon our achievement of annual performance measures that are aligned with the business strategy and shareholders' interests.
<b>Long-term Elements</b>	<b>How Objectives Are Met</b>
Stock Options	Performance-based compensation that delivers value to executives based on long-term stock price appreciation.
Restricted Stock	Performance-based compensation that enhances shareholder value because vesting is tied to achievement of current year corporate performance measures, and because value varies based on long-term total shareholder return.
Performance Shares	Performance-based compensation that delivers shares of our stock only if we perform well relative to peers over a multi-year period, and therefore aligns named executives' interests with our business strategy and long-term shareholder return.
Retirement Programs	Serve as a retention tool for executives and help us attract mid-career top executive talent from other companies.
Severance and Change-in-Control Arrangements	Promote focus and commitment by executives during a potential change-in-control; help retain executives in light of significant business combinations in the financial services industry.

We believe our executive compensation program aligns named executives with short- and long-term current business objectives, effectively motivates named executives to create long-term shareholder

value, pays competitively with our peers and provides strong incentives for named executives to join and remain at Washington Mutual.

### **How We Set Compensation Levels**

#### *Peer Group Analysis*

Each year, with the assistance of its consultant, the Committee reviews the composition of the peer group it uses to benchmark compensation, and the compensation levels, programs and practices of those peers, as part of the Committee's process of setting executive compensation. The Committee used the peer group listed below, comprising our primary competitors in our major business lines and for executive talent, in connection with 2007 executive compensation decisions:

Bank of America

Bank of New York

Capital One Financial Corp.

Citigroup

Countrywide Financial

Fifth Third Bancorp

JPMorgan Chase & Co.

KeyCorp

National City Corp.

PNC Financial Services Group

Suntrust Bank

U.S. Bancorp

Wachovia

Wells Fargo & Company

The Committee annually evaluates the companies in the peer group and adjusts the list as appropriate. For 2007, the Committee added Capital One Financial Corp. to the peer group. The Committee determined Capital One to have become a primary competitor for two principal reasons: our recent expansion into the credit card business, a core business for Capital One, and Capital One's expansion into banking. The following table shows the comparator data reviewed by the Committee when it approved 2007 annual executive compensation elements in January 2007.



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Element	WaMu	Peer Median	Peer Average
Market Capitalization (in billions)	\$ 42.70	\$ 30.66	\$ 84.25
2005 Assets (in billions)	343.75	177.39	441.07
2005 Revenues (in billions)	21.33	14.33	32.86

The Committee reviews both current year and three-year average peer compensation data when it makes compensation decisions. The use of three-year averages minimizes the potential impact on the Committee's decision-making process of large upswings or downswings in one-year data as a result of extraordinary compensation amounts that may be paid in a given year by a peer or group of peers.

*Compensation Benchmarking and Other Factors in Setting Compensation*

A primary compensation objective is to attract, develop and retain high-quality executive officers selected from a national, and in some cases, international, talent pool. To help achieve this objective, as a guideline, we target executive cash compensation (salary and annual bonus) at the median (50th percentile), and separately target long-term equity incentive compensation at the 75th percentile, compared to our peers. We target cash compensation at the 50th percentile to be comparable to peer companies. We consider compensation "comparable" if it is within 10% of the target amount. We believe the 75th percentile, more than just comparable to our peers, is appropriate for our long-term equity incentives because of the great emphasis we place on at-risk compensation that is directly tied to increasing shareholder value.

The Committee does not rigidly set executive compensation in accordance with these target guidelines. Actual compensation can and does vary from target levels depending on Company and individual performance. The Committee believes the proper exercise of its role of overseeing executive compensation requires it to evaluate executive performance and compensation levels by taking into account all relevant factors, of which peer data is only one. The Committee also considers Company performance and individual qualitative factors such as the executive's performance, business unit performance, previous experience, incumbent time in his or her job and internal pay equity. There is no formal weighting of these internal factors or the market data used by the Committee in making its decisions, and typically specific factors are not called out as the basis for a particular decision.

The following table shows the actual 2007 target total cash and long-term equity incentive ("LTI") amounts the Committee approved for each named executive, and where those amounts fall relative to peer targets (above or below the 50th or 75th percentile, as applicable). The 2007 LTI award values differ from the sums of the amounts shown for each named executive in the Grant Date Fair Value of Stock and Option Awards column of the Grants of Plan-Based Awards Table at page 106 because the amounts shown at page 106 are the associated accounting expense under FAS 123R. The Committee does not use accounting expense as a starting point for determining LTI awards.

Named Executive	2007 Target Cash (Actual)	2007 Target Cash (Benchmark)	2007 LTI (Actual)	2007 LTI (Benchmark)
Kerry K. Killinger	\$ 4,650,000	Below 50th	\$ 11,500,000	At 75th
Thomas W. Casey	1,874,880	At 50th	4,000,000	Above 75th
Stephen J. Rotella	3,724,880	Above 50th	6,000,000	At 75th
James B. Corcoran	1,474,140	At 50th	1,500,000	At 75th
Ronald J. Cathcart	1,651,680	At 50th	1,750,000	Above 75th
Fay L. Chapman	1,060,320	Above 50th	1,350,000	At 75th

Variances from our benchmarking guidelines for some named executives, as shown in the table above, were due to the following reasons:

We set Mr. Killinger's target cash compensation below the 50th percentile guideline because we believe it is less important for CEO cash compensation to be comparable to peers given the substantial portion of CEO total direct compensation delivered in the form of long-term equity incentive compensation.

We set Mr. Casey's long-term incentive compensation value above the 75th percentile primarily due to internal pay equity considerations, in order to place his compensation above other function heads given the importance of the CFO role to our Company.

We set Mr. Rotella's target cash compensation above the 50th percentile because that level of compensation was necessary to recruit Mr. Rotella when he joined us as a mid-career senior executive from one of our competitors, a major diversified financial institution.

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We set Mr. Cathcart's long-term incentive compensation value above the 75th percentile primarily due to internal pay equity considerations based on the broad scope of his role relative to other functional unit leaders.

We set Ms. Chapman's target cash compensation above the 50th percentile as a reflection of her long tenure and due to internal pay equity considerations given her position as a Senior Executive Vice President.

### *Use of Tally Sheets*

The Committee receives and reviews rewards profiles that summarize each executive's total compensation at each regularly scheduled Committee meeting. These profiles are commonly referred to as "tally sheets." The Committee did not use tally sheets as a primary basis to determine 2007 executive compensation amounts. However, tally sheets are an important reference tool for the Committee because they demonstrate how our executive compensation program is working in practice by summarizing, for each executive, the overall total compensation awarded in the past and the anticipated future value of our various compensation programs. The anticipated future value shown on the tally sheets includes the projected value of compensation payable upon separation of employment under various circumstances, including death or disability, retirement and voluntary or involuntary separation. In this regard, the tally sheets assist the Committee in identifying factors that may be taken into account in setting elements of compensation, such as internal pay equity, retention risk (demonstrated in part by the current retentive value of past equity awards) and the value of past awards both on a long- and short-term basis.

### *Internal Pay Equity Analysis*

Internal pay equity, meaning whether an executive's compensation appropriately reflects the role, scope and complexity of the executive's position relative to other executives, is an objective of our executive compensation program. While the structure of Mr. Killinger's compensation was similar to that of other named executives in 2007, his total compensation amount is significantly more than the other named executives as a reflection that he is most accountable for the overall performance of the Company. Although the percentage of total direct compensation that is "at risk" varies depending on each named executive's level of influence over specific business unit and overall corporate results, we do not view these differences as material. We consider compensation to be "at risk" when its payment is not fixed or guaranteed, but rather depends upon factors such as satisfaction of performance measures or stock price appreciation. The following table shows the percentages of 2007 named executive total direct compensation that were "at risk" and how total direct compensation was allocated among its three component parts of base salary, target bonus and long-term equity incentive ("LTI") award value.

**2007 Named Executive Officer Total Direct Compensation ("TDC")\***

Named Executive	Total % At Risk	% of TDC that is LTI	% of TDC that is Target Bonus	% of TDC that is Fixed (Base Salary)
Kerry K. Killinger	94%	71%	23%	6%
Thomas W. Casey	89	68	20	11
Stephen J. Rotella	91	62	29	9
James B. Corcoran	79	50	29	21
Ronald J. Cathcart	83	51	31	17
Fay L. Chapman	69	56	13	31

\*

Due to rounding, certain totals differ slightly from the sum of the component parts shown in the table.

## Discussion and Analysis of Compensation Elements

### *Base Salary*

The Committee reviews base salaries each year to ensure they remain competitive and appropriately reflect individual performance and the complexity of each executive's role and responsibilities. Mr. Killinger did not receive a base salary increase for 2007 and has not received an increase since 1999 in order to maintain the tax deductibility of his salary. Other named executives received regular annual base salary increases for 2007 of up to 4.8% of 2006 amounts. No named executive received a base salary increase for 2008.

### *Annual Incentive Bonus*

The target cash incentive bonus is one of three elements of total direct compensation approved by the Committee each year, and it represents less than half of total direct compensation for each named executive. As shown in the table above, our long-term equity incentive compensation program represents at least 50% of each named executive's total direct compensation (over 70% for our CEO) and is directly linked to stock price and total shareholder return. The incentive bonus program is designed to align compensation with achievement of annual corporate performance measures that reinforce our near-term business strategies and shareholders' interests. We set an annual target cash incentive bonus for each named executive with payment based on annual Company performance measures established by the Committee pursuant to the Company's Leadership Bonus Plan. Mr. Killinger's target bonus increased to 365% of his base salary for 2007 from 350% in 2006. We increased his target bonus in connection with the elimination of Company-paid perquisites, discussed more fully below. Target bonuses for other named executives changed in amounts ranging from a 9% decrease to a 4% increase, as a percentage of base salary.

### *Performance Measures*

Cash bonus amounts actually paid to our named executives depend upon our corporate results compared to a pre-established formula of performance measures that we believe are drivers for creating shareholder value and achieving our annual strategic goals. Each year the Committee selects performance measures that are typically tied to core measures of corporate operating performance and are challenging but realistic given the expected operating environment at the time they are established. Because our general guideline is to target executive cash compensation (salary and target cash bonus) at the median compared to our peers, the Leadership Bonus Plan performance measures, including the measures for 2007 performance, are generally set to align with our business plan for the year so that bonuses will pay out at 100% of target when the business plan is met. Based on our performance in 2003 and 2004, we paid bonuses to our then-current named executives at 98.1% and 64.2% of target levels, respectively. In 2005 and 2006, our performance against the applicable measures exceeded expectations and resulted in bonus payouts at 118.5% and 116.4% of the respective target amounts. As explained below, our 2007 financial results in the context of unprecedented challenges in the mortgage and credit markets resulted in a total weighted payout percentage of 32.6% under the 2007 Leadership Bonus Plan.

We determined the amount of bonuses paid in January 2008 (for 2007 performance) based on our performance against the following four measures established by the Committee in January 2007. The mix of measures was different in 2007 as compared to 2006. For 2007, we added a noninterest income measure, as a complement to the noninterest expense measure, to balance our focus on both generating income and reducing expense. Also for 2007, we measured customer loyalty rather than customer satisfaction as a reflection of the link between customer loyalty and financial results.

*Earnings-per-share.* The first 2007 performance measure was earnings-per-share, or "EPS", weighted at 40%, with target EPS depending on the interest rate environment within which our

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business operated in 2007. The target that applied for the year was determined according to a matrix approved by the Committee in January 2007. The matrix consisted of numerous alternative EPS targets that applied depending on the interest rate conditions that existed over the course of the year, as indicated by the applicable short-term interest rates and the spread between short-term and long-term rates. After the end of 2007, we referred to the EPS matrix to determine which EPS target applied given the year's interest rate environment. We do not disclose the EPS target matrix because it is confidential and competitively sensitive information.

*Noninterest Expense.* The second performance measure was noninterest expense, weighted at 25%, which was aligned with our strategic goal of reducing expenses and increasing efficiency to remain competitive. Target noninterest expense for 2007 was \$8.45 billion. Our 2007 noninterest expense as measured under the plan was \$8.68 billion. The following table shows the percentage payouts for this measure at different levels of noninterest expense.

Noninterest Expense (in billions)	Payout Percentage	Noninterest Expense (in billions)	Payout Percentage
\$ 7.85	150%	\$8.85	70%
\$ 7.95	140%	\$8.95	60%
\$ 8.05	130%	\$9.05	50%
\$ 8.15	120%	\$9.15	40%
\$ 8.30	110%	\$9.25	30%
\$ 8.45	100%	\$9.35	20%
\$ 8.60	90%	\$9.45	10%
\$ 8.75	80%	>\$9.55	0%

*Noninterest Income.* The third performance measure was noninterest income, weighted at 25%, which was aligned with our strategic goal of increasing income as well as reducing expenses. Target noninterest income for 2007 was \$7.05 billion. Our 2007 noninterest income was \$6.04 billion. The following table shows the percentage payouts for this measure at different levels of noninterest income.

Noninterest Income (in billions)	Payout Percentage	Noninterest Income (in billions)	Payout Percentage
\$ 7.65	150%	\$6.65	70%
\$ 7.55	140%	\$6.55	60%
\$ 7.45	130%	\$6.45	50%
\$ 7.35	120%	\$6.35	40%
\$ 7.20	110%	\$6.25	30%
\$ 7.05	100%	\$6.15	20%
\$ 6.90	90%	\$6.05	10%
\$ 6.75	80%	\$5.95	0%

*Customer Loyalty.* The fourth performance measure was customer loyalty, weighted at 10%, which was determined according to a proprietary measurement system. High levels of customer service, which drive customer loyalty, remain an important aspect of our consumer-oriented business philosophy. We do not publicly disclose overall targets or specific criteria comprising the customer loyalty measure because it is confidential and competitively sensitive information. Our performance in 2007 improved our overall customer loyalty as compared to 2006, but not enough to achieve a 100% payout for this measure.

If our performance for any measure falls between stated percentiles, we interpolate to determine the applicable payout percentage. As shown in the following table, our performance against each of the



four 2007 performance measures resulted in a total weighted payout percentage of 32.6% of target bonus amounts.

Performance Measure	Percentage of Target Payout Based on 2007 Company Performance	Weighting	Weighted Payout Percentage
Earnings-per-share	0%	40%	0%
Noninterest Income	9.2	25	2.3
Noninterest Expense	84.0	25	21.0
Customer Loyalty	92.8	10	9.3
<b>Total Weighted Payout Percentage</b>			<b>32.6%</b>

Our performance results used to calculate EPS and noninterest expense under the 2007 Leadership Bonus Plan excluded the effects of specific restructuring and non-cash goodwill impairment charges we reported in a Current Report on Form 8-K filed with the SEC on December 10, 2007. These charges were excluded because they were not part of our business plan when we established the 2007 Leadership Bonus Plan and they masked management's achievements in controlling noninterest expense in our operations. If we had not excluded the charges from the calculation, our performance on noninterest expense would have been below threshold, resulting in a weighted payout percentage of 0% for that performance measure and a total weighted payout percentage at 11.6% of target amounts. Excluding the charges from the calculation of EPS performance had no effect on bonus payouts, as EPS performance was below threshold whether or not the charges were excluded.

#### *2007 Bonus for Chief Executive Officer*

Our CEO, Kerry Killinger, did not accept a bonus for 2007. Our 2007 performance would have resulted in a payout to Mr. Killinger of \$1,189,900 (32.6% of his 2007 target bonus of \$3,650,000). The other named executives received bonus payouts equal to 32.6% of their target bonuses, other than Ms. Chapman, who received a bonus payout at 100% of target under the terms of her severance agreement which is discussed below. The amount of Mr. Killinger's forgone 2007 bonus will be taken into account in the calculation of his benefits under our Executive Target Retirement Income Plan as though he had received the bonus. Also, as more fully discussed below, Mr. Killinger not accepting a bonus had no effect on the percentage of his 2007 restricted stock awards that is eligible to vest, which is based on our total weighted performance under the 2007 Leadership Bonus Plan performance measures.

#### *2008 Bonus Plan Design*

The Committee varies the performance measures and the weights assigned to each performance measure from year to year based on current year business objectives. For 2008 bonuses the Committee selected the following performance measures and relative weights which apply to executives and almost 3,000 of our senior managers: net operating profit: 30%, noninterest expense: 25%, depositor and other retail banking fees: 25%, and customer loyalty: 20%. Net operating profit will be calculated before income taxes and excluding the effects of loan loss provisions other than related to our credit card business and expenses related to foreclosed real estate assets. Noninterest expense will be calculated excluding expenses related to business resizing or restructuring and expenses related to foreclosed real estate assets. For each of these performance measures, the Committee established a range of achievement levels from zero to 150% of target. Like the 2007 plan, the 2008 Leadership Bonus Plan bonus payout targets range up to 365% of 2008 base salary, depending on position. In evaluating financial performance, the Committee may adjust results to eliminate the effects of charges for restructurings, discontinued operations, extraordinary items and items of gain, loss or expense determined to be extraordinary or unusual in nature or infrequent in occurrence or related to the disposal of a segment or a business or related to a change in accounting principle.

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The foregoing measures of operating performance are critical to the future growth and profitability of the Company. In selecting and defining the net operating profit performance measure for 2008, a period when the Company was expecting to experience significantly elevated loan loss provision and foreclosed asset expense from its single-family residential mortgage loan portfolio, the Committee was focused on sustaining and growing the Company's top-line revenues and controlling other expenses. Sustaining and growing top-line revenues and controlling other expenses were seen as important to achieving the following objectives: (a) enabling the Company to return to longer-range earnings expectations after these elevated credit costs subside, and (b) helping ensure that the fundamental drivers of the Company's long-term franchise value would not be materially diminished during the period of elevated credit costs in its mortgage loan portfolios. The Committee believed that these objectives would provide a foundation for restoring shareholder value. The Committee also will evaluate executive performance with respect to credit risk management in light of the dislocation in the housing and credit markets and the related impact on our financial results. Accordingly, after the end of 2008, the Committee will exercise its discretion under the 2008 bonus plan to determine the final cash bonus payouts for executive officers by:

- 1) reviewing and considering performance results for the four pre-established Company performance measures noted above;
- 2) reviewing other appropriate factors and measures of Company financial performance; in particular, the Committee will subjectively evaluate Company performance in credit risk management and other strategic actions that impact overall corporate profitability; and
- 3) evaluating each executive's individual performance during 2008 to determine whether it is appropriate to adjust the executive's final bonus payout from the amount that would be payable based solely on the Committee's assessment of Company performance under steps (1) and (2) above.

The Committee intends for this structure to maintain the Company's longstanding practice of tying annual incentive compensation to achievement of critical corporate operating performance goals. The first step above provides the basis for the Committee to reward executive performance against the four objective performance measures and begins the analysis of determining the appropriate bonus payouts. As a second step the Committee will judge how well our executive management team addressed the challenges in the housing, mortgage and credit markets and the impact of those challenges on our financial results. The Committee considered the unprecedented volatility in the markets, the possibility of further interest rate actions or legislation which would significantly impact our business and financial results, and the need for management to maintain a broad and flexible perspective in responding to the business environment. Therefore, the Committee determined that establishing specific, quantified performance measures for credit risk management and overall profitability in advance presented the risk of setting incentives that, when viewed in retrospect after the end of the year, might be inappropriate or misdirected. Accordingly, the Committee determined that it would be best to evaluate this aspect of performance after the end of the year in light of actual events and market conditions during the year. As a third step the Committee will consider each executive's individual performance in determining the appropriate bonus payout. The Committee remains committed to paying for performance and it will exercise its discretion in alignment with that principle when determining 2008 executive bonuses.

### ***Long-Term Equity Incentive Compensation***

We design our long-term equity incentive programs to retain named executives and motivate them to create long-term shareholder value. We believe in paying competitively, and to do so, we do not reduce current year equity awards based on value realized from prior awards. By changing the mix of equity vehicles, we can emphasize one or more compensation objectives each year based on business



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objectives, market conditions and compensation trends. For 2007, we granted three forms of long-term equity incentive compensation, each promoting our objectives in different ways:

*Stock Options.* Stock options enhance retention by vesting over time, and promote the creation of shareholder value by tying the named executives' ultimate realized value to stock price appreciation.

*Restricted Stock.* Restricted stock enhances retention by vesting over time, and promotes the creation of shareholder value by focusing named executives on total shareholder return. In addition, performance criteria associated with vesting helps to drive achievement of our business goals and objectives and makes awards tax deductible under Section 162(m) of the federal tax code.

*Performance Shares.* Performance shares enhance retention due to a three-year performance cycle and promote the creation of shareholder value because they are ultimately issued only if we perform well relative to our peers according to an established performance matrix.

As in prior years, for 2007 the Committee offered named executives choices for allocating their total equity award among these three vehicles. The performance share component represented 30% of the award in all three choices, with the relative weighting of stock options and restricted stock varying. As in 2006, for 2007 the Committee fixed the performance share component at 30% to allocate the same proportion of each named executive's equity award to the riskiest vehicle. The choices for allocating the remaining 70% of their awards were as follows:

	Choice 1	Choice 2	Choice 3
Restricted Stock	35%	45%	25%
Stock Options	35%	25%	45%
Performance Shares	30%	30%	30%

When establishing each executive's total long-term equity incentive award, the Committee first sets an aggregate dollar amount for the award. The aggregate dollar amount aligns with our guideline of targeting long-term equity incentive compensation at the 75th percentile of peer companies, except where other factors discussed above lead to a different relative position.

After determining an award value, we convert the aggregate dollar amount for each award into a number of shares of restricted stock, performance share awards and stock options, as may be applicable from year to year. To convert the stock option award value into a number of stock options, we use an option valuation model which establishes a binomial value per stock option based on a number of factors, such as risk-free interest rate, stock volatility over the term of the option, the length of the option term, dividend yield, the exercise price of the option and the market price of our stock. For 2007, our option valuation model produced a binomial value of \$8.08 per stock option, which we used to convert the stock option award value into a number of stock options. We convert the restricted stock award value and performance share award value into a number of shares by dividing the award value by a representative market price of our stock derived over a period prior to the grant date, with a discount factor applied to reflect the risk associated with any applicable performance criteria. For 2007, we used \$38.70 per share as the conversion price for restricted stock and \$36.87 per share for performance shares. These conversion methodologies allow us to determine the number of shares subject to each form of award before seeking Committee approval, and also to avoid the effects of events impacting our stock price around the actual time of grant.

### *Stock Options*

Given our relatively stable business and operating environment in early 2007 when we granted 2007 awards, our compensation objectives for stock options were relatively straightforward: to promote

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retention and align named executives with shareholders through stock price appreciation over time. Therefore, we awarded 2007 annual stock options with terms consistent with our historical practice. The 2007 options vest in three equal annual installments beginning on the first anniversary of the grant date and have a 10-year term.

### *Restricted Stock*

We implemented a number of changes in 2007 to our restricted stock program for named executives. For 2007 awards, dividends payable on restricted stock are reinvested in additional shares that will be subject to the same restrictions and risk of forfeiture as the underlying shares. For previously granted awards, other than employment sign-on awards, quarterly dividends continue to be paid in cash. Also, for 2007 awards, we conditioned vesting on achievement of the Company performance measures used to determine our 2007 bonus payouts under the Leadership Bonus Plan, as described beginning at page 89 above. Therefore, the 2007 restricted stock awards will vest over three years, but only to the extent of the total weighted payout percentage under the 2007 Leadership Bonus Plan. As a result, for named executives other than Ms. Chapman, 67.4% of the 2007 restricted stock awards were forfeited and the remaining 32.6% vest over three years from the date of grant. The following table shows the number of shares each named executive will retain, subject to the three-year vesting schedule, and the number of shares each will forfeit, in each case including dividends accrued since the grant date.

Named Executive	Shares of 2007 Restricted Stock Eligible to Vest	Shares of 2007 Restricted Stock Forfeited
Kerry K. Killinger	46,644	96,435
Thomas W. Casey	16,222	33,539
Stephen J. Rotella	24,351	50,345
James B. Corcoran	6,070	12,550
Ronald J. Cathcart	5,512	11,396
Fay L. Chapman	17,443	0

Under the terms of our severance agreement with Ms. Chapman, discussed more fully below, the performance conditions applicable to Ms. Chapman's 2007 restricted stock award were waived meaning that 100% of her 2007 award is eligible to vest over the three-year vesting schedule.

### *Performance Shares*

In 2007 and prior years, performance shares were a significant component of our executive long-term equity incentive program, with 30% of the value of each named executive's total award being in the form of performance shares. The 2007 performance share awards were stated in terms of a target payout, and the actual payout can range from zero to 250% of target, depending on our performance relative to the performance of our peers. The target payout is at the 60th percentile of the peer group companies, and is payable at 100% of the contingent award. The threshold payout is at the 30th percentile of the peer group companies, and is payable at 25% of the contingent award. There is no payout if our performance is below the 30th percentile of peer group companies. The peer group for this purpose consists of the financial services companies comprising the Standard & Poor's Financial Index at the time of the award, excluding real estate investment trusts and companies that cease to be public companies during the applicable performance cycle. We use this broader peer group for the three-year performance cycle, as opposed to the smaller peer index used to benchmark compensation, because the Committee believes the broader group is a more appropriate benchmark for corporate performance since it encompasses a wider variety of business models and is less influenced by consolidations in the financial services industry and anomalous results of individual companies. A list of

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the Standard & Poor's Financial Index companies in the peer group for the awards in the 2004-2006 performance cycle, for which performance was measured for possible payout in 2007, is included below.

We will issue performance shares, if at all, at the end of a three-year period, called a performance cycle. At the end of the performance cycle, earned awards together with dividends on the earned shares that are reinvested in our common stock are paid out in unrestricted shares of our common stock (or cash at the discretion of the Committee). For awards made in 2007, the performance cycle is 2007-2009. Over the performance cycle, we measure our performance relative to our peers with respect to earnings-per-share growth, total shareholder return and average return on tangible common equity. Each of the performance measures has equal weight in determining the payout. Towers Perrin evaluates our performance under the performance share program on a quarterly basis. To measure overall performance, the companies in the peer group (including our Company) are stack-ranked for each measure, and then the sum of their rankings on each measure is used to determine final rank. The following schedule sets forth the payout amounts for our relative performance against peers:

<b>Percentile Rank Among Peers for: Earnings-Per-Share Growth, Total Shareholder Return, and Average Return on Tangible Common Equity</b>	<b>Payout as a Percentage of Target</b>
90th or Above	250%
85th	225
80th	200
75th	175
70th	150
60th	100
50th	75
40th	50
30th	25
Below 30th	0

If our relative ranking falls between stated percentiles, the Committee interpolates to determine the payout percentage. For example, if we rank in the 55th percentile for the aggregate sum of our rankings in each of the three performance measures, the payout would be 87.5% of target.

The performance shares program reflects our objective to link compensation to performance, as evidenced by the payout of 0% for the performance cycles that ended in 2005, 2006 and 2007.

**Standard & Poor's Financial Index Companies in the Performance Share Peer Group for Awards in the 2004-2006 Performance Cycle**

ACE Ltd  
AFLAC Inc  
Allstate Corp (The)  
Ambac Financial Group Inc.  
American Express Co  
American International Group Inc  
Ameriprise Financial Inc  
Aon Corp.  
Bank of America Corp  
Bank of New York Co Inc. (The)  
BB&T Corp  
Bear Stearns Companies Inc (The)  
Capital One Financial Corp.  
Chicago Mercantile Exchange Holdings Inc.  
Chubb Corp (The)  
Cincinnati Financial Corp  
CIT Group Inc.  
Citigroup Inc.  
Comerica Inc  
Commerce Bancorp Inc.  
Compass Bancshares Inc.  
Countrywide Financial Corp  
E\*TRADE Financial Corporation  
Federal Home Loan Mortgage Corp.  
Federated Investors Inc.  
Fifth Third Bancorp  
First Horizon National Corp  
Franklin Resources Inc  
Goldman Sachs Group  
Hartford Financial Services Group Inc. (The)  
Huntington Bancshares Inc  
Janus Capital Group Inc  
JPMorgan Chase & Co  
KeyCorp  
Legg Mason Inc  
Lehman Brothers Holdings Inc  
Lincoln National Corp  
Loews Corp  
M&T Bank Corp  
Marsh & McLennan Companies Inc.  
Marshall & Ilsley Corp  
MBIA Inc.  
Mellon Financial Corp  
Merrill Lynch & Co Inc  
Metlife Inc.  
MGIC Investment Corp  
Moody's Corp.  
Morgan Stanley  
National City Corp  
Northern Trust Corp  
PNC Financial Services Group Inc.  
Principal Financial Group Inc.  
Progressive Corp (The)  
Prudential Financial Inc  
Regions Financial Corp  
Safeco Corp  
Schwab (Charles) Corp  
SLM Corp  
Sovereign Bancorp Inc.

State Street Corp  
SunTrust Banks Inc.  
Synovus Financial Corp.  
T. Rowe Price Group Inc  
Torchmark Corp  
Travelers Companies Inc (The)  
U.S. Bancorp  
Unum Group  
Wachovia Corp  
Washington Mutual Inc  
Wells Fargo & Co  
XL Capital Ltd  
Zions Bancorporation

*Timing of Annual Equity Grants*

Our standard practice is to grant annual equity awards on the second business day following release of year-end earnings. We have followed this practice for several years for two reasons. It ensures that our publicly-reported financial results have been absorbed by the market when the exercise price of stock options, which is always our stock's closing market price on the grant date, is set. It also permits the Committee to consider our final year-end results when approving equity awards.

*2005 Special Restricted Stock Award Based on Five-Year Strategic Plan*

In 2005, the Committee awarded special performance-based restricted stock to certain named executives in order to align the executives' interests with our new five-year strategic plan and enhance retention. Messrs. Killinger, Rotella, Casey and Cathcart and Ms. Chapman received this award. The Committee considered the total compensation package of each executive and how critical their efforts were expected to be in achieving the five-year plan when determining the number of shares to award. Mr. Corcoran did not receive this award because he was not with us in 2005. Between 0% and 100% of these awards will vest shortly after December 31, 2009 depending upon our performance, as measured by our average annualized return on tangible common equity over the period beginning on July 1, 2005 and ending on December 31, 2009. We must achieve a threshold performance of 50% of target for any payout to occur. When final results are known, the payout matrix established at the time of grant will be used to determine the number of shares awarded. Dividends payable on these shares are reinvested

in shares of our common stock that have the same restrictions as the underlying restricted shares. We have no current plans to make similar awards in the future.

*2008 Long-Term Equity Incentive Awards*

Due to the significant erosion in shareholder value in the latter half of 2007, providing strong performance-based incentives to our executive officers, including the named executives and particularly the Chief Executive Officer and the Chief Operating Officer, was a primary compensation objective for the 2008 long-term equity incentive awards. Moreover, due to the current unprecedented challenges in the mortgage and credit markets, retaining executive officers and other key employees, including the named executives, also was a primary compensation objective for the awards. In determining the 2008 equity awards, the Committee replaced the performance share component of our long-term equity incentive program with additional stock options. Although performance shares have been used in recent years, including 2007, the Committee concluded that for 2008, the evaluation of Company performance should not be limited to a few discrete criteria but instead that named executives should be motivated to proactively identify and address a wide range of initiatives to restore and create shareholder value through increased stock price. The Committee concluded that stock options with the carefully established vesting terms described below better achieve this objective.

As discussed below, Mr. Killinger's 2008 award consisted solely of stock options. The 2008 awards made to the other named executives consisted of stock options and restricted stock. Since she is no longer an executive officer, and in accordance with the terms of her severance agreement discussed below, Ms. Chapman did not receive a 2008 equity award.

*2008 Long-Term Equity Incentive Award to Chief Executive Officer*

The Committee's primary compensation objective for Mr. Killinger's 2008 equity award was to provide a strong incentive to restore shareholder value. Accordingly, Mr. Killinger's 2008 equity award consisted entirely of performance-based stock options with vesting terms tied to the price of our common stock achieving certain thresholds. Mr. Killinger's 2008 long-term equity incentive award value is approximately 15% greater than his 2007 award value, which resulted in a grant of 3.2 million stock options. Fifty percent of the stock options will vest upon the *later of* (i) the third anniversary of the grant date, or (ii) the NYSE-reported trading price of our common stock closing at \$26 or more per share for 15 consecutive trading days. The remaining 50% of the stock options will vest upon the *later of* (i) the fourth anniversary of the grant date, or (ii) the NYSE-reported trading price of our common stock closing at \$35 or more per share for 15 consecutive trading days. Vesting may also be accelerated upon other events specified in our Amended and Restated 2003 Equity Incentive Plan and standard form of option award agreement, such as a qualifying change-in-control transaction, a qualifying retirement, death or permanent disability. The stock options have a term of seven years.

*2008 Long-Term Equity Incentive Awards to Other Named Executives*

Each other named executive, other than Ms. Chapman, received a 2008 stock option grant with an award value approximately equal to the aggregate award value of his total 2007 long-term equity incentive award, and a 2008 restricted stock grant in an amount determined by the Committee's assessment of the executive's individual performance and the severity of the retention risk associated with him based in part on the significant decline in the current value of the executive's prior equity awards. The restricted stock will vest in two equal installments on the second and third anniversaries of the grant date, subject to our satisfying one of two 2008 performance conditions established to make the expense associated with the awards tax deductible under Section 162(m) of the Internal Revenue Code.

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As with Mr. Killinger, the Committee wanted to provide Mr. Rotella, President and Chief Operating Officer, with a strong incentive to restore shareholder value. Therefore, Mr. Rotella's stock options were granted on terms identical to Mr. Killinger's, as discussed above. The Committee determined to provide comparable stock price incentives for equity awards to the other named executives receiving awards, and also placed a greater emphasis on the retention objective for those equity awards. Therefore, stock options granted to Messrs. Casey, Corcoran and Cathcart were granted with stock price vesting terms similar to those under the options granted to Messrs. Killinger and Rotella, except that the options granted to Messrs. Casey, Corcoran and Cathcart will vest 100% on the *earlier of* (i) the third anniversary of the grant date or (ii) the NYSE-reported trading price of our common stock closing at \$26 or more per share for 15 consecutive trading days, and likewise are subject to accelerated vesting upon certain other events specified in our Amended and Restated 2003 Equity Incentive Plan and standard form of option award agreement.

The number of stock options and shares of restricted stock awarded to named executives in 2008 is significantly higher than the number awarded in recent years due primarily to the low valuation per option and restricted share, respectively, resulting from the current relatively low market price of our common stock and, for the stock option grants, the shift in the mix of equity award components in favor of stock options as a replacement for performance shares for a significantly higher percentage of the total award value. Higher overall award values also increased the number of stock options and shares of restricted stock awarded to named executives in 2008.

### *Perquisites*

We eliminated Company-paid perquisites for our executive officers at the end of 2006. For security reasons and to increase his efficiency, our Board of Directors continues to encourage Mr. Killinger to use our aircraft for business-related and personal transportation. However, beginning in 2007, Mr. Killinger reimburses us for our aggregate incremental cost of his personal use of corporate aircraft.

### *Post-Employment Arrangements*

We provide several post-employment arrangements that reflect our goal to provide competitive retirement packages. These arrangements also help us attract and retain top executive talent and focus our named executives on long-term performance by mitigating possible concerns over industry consolidation. In the past several years, we have been able to attract experienced executives both nationally and internationally, and we believe our post-termination arrangements have been an important recruiting and retention tool.

We maintain several retirement plans in addition to our tax-qualified, broad-based WaMu Pension Plan and WaMu Savings (401(k)) Plan. The other retirement plans in which named executives participate are the Supplemental Employees' Retirement Plan (the "*SERP*"), the Supplemental Executive Retirement Accumulation Plan (the "*SERAP*"), and the Executive Target Retirement Income Plan (the "*ETRIP*"). In addition, we maintain a deferred compensation plan that is available to named executives and other highly compensated employees. Each of our retirement plans is described in detail beginning at page 114.

### *Nonqualified Retirement Plans*

As we have grown, our executive retirement plan program has evolved to remain competitive with an increasingly higher caliber of peer companies in the financial services sector. As a result, named executives continue to participate in one or more executive retirement plans, in addition to the broad-based WaMu Pension Plan and WaMu Savings Plan.

The SERP is an excess plan that makes up for WaMu Pension Plan limitations imposed by the Internal Revenue Code (\$225,000 in 2007). In general, the provisions contained in this plan mirror the

WaMu Pension Plan, including benefit accrual rates. The SERAP was an existing executive program, which we limited to lower-level executives when we implemented the ETRIP on January 1, 2004. Because participants had vested contractual rights under the SERAP, we did not eliminate current balances for those eligible to participate in the SERAP at that time. However, to prevent plan participants from receiving duplicate retirement benefits, the ETRIP provides for an offset for benefits under the WaMu Pension Plan, the SERP and the SERAP, and Company contributions under the WaMu Savings Plan. As a result, the ETRIP generally establishes the maximum retirement benefit payable to the named executives, although that benefit amount may be paid in part through the other plans mentioned. The ETRIP, SERP and SERAP are more fully described beginning at page 115.

#### *Executive Target Retirement Income Plan Amendments*

The Committee recently asked Towers Perrin for a comprehensive review of executive retirement plans. The results of the review indicated that the aggregate benefits payable under our executive retirement plans could be somewhat greater than our peers provide. As a result, in January 2008 the Committee approved amendments to the ETRIP to exclude from participation new named executives hired or otherwise made eligible after December 31, 2007. While the Committee does not establish a competitive market target for retirement plans and it is often difficult to gauge exact comparisons of retirement benefits, by person, due to age and service factors inherent in retirement plans, in its review the Committee determined that the ETRIP may provide a greater level of retirement benefits relative to our peers than was originally intended. As a result, the Committee approved an amendment to the plan providing that, effective December 31, 2012, participants will cease to accrue employment service credits for benefits and vesting purposes, except in the case of a change-in-control, in which case participants would receive an additional three years of service credit as they would before the amendments. In connection with this amendment, the Committee also approved other amendments affecting the benefit calculation formula which are intended to mitigate erosion of current benefits. Effective December 31, 2012, benefits for each participant no longer will be reduced by (i) future Company contributions or credits the participant receives under our other general and executive retirement benefit plans and the WaMu Savings Plan, or (ii) the effects of decreases in base salary and bonus during the five-year measurement period.

#### *Deferred Compensation Plan*

We also sponsor an unsecured non-qualified plan known as the Deferred Compensation Plan, which allows named executives and certain other highly compensated employees to defer all or a portion of their base salary, bonus, stock option gains, earned performance shares and vested shares of restricted stock. Balances in the plan receive earnings accrual credits from among several plan options, all of which are described at page 119. Other than earnings accruals, all credits to the Deferred Compensation Plan represent an executive's compensation previously earned and deferred; we do not provide any matching or similar credits other than dividend equivalents for balances with earnings accrual credits based on the phantom stock method. The plan was designed to allow named executives to defer some of their current income to help them with tax planning, and to help us attract and retain top named executives by providing retirement benefits that are competitive within our peer group. As more fully explained at page 119, in 2007 we allowed participants to make a one-time election to accelerate distributions of previously deferred compensation under the transition rules of Internal Revenue Code Section 409A. Distributions as a result of these elections will begin in July 2008.

#### *Employment, Change-in-Control and Severance Arrangements*

##### *Employment and Change-in-Control Arrangements*

We provide named executives with agreements that provide for certain specified benefits upon a change-in-control of the Company. These agreements are very useful tools that help us attract and



retain our key employees, including the named executives. Such agreements were put in place at various times and reflect a variety of different considerations. We have provided these change-in-control agreements primarily as a result of the Committee's and its consultant's periodic assessments of compensation practices in the financial services industry, and in recognition that they are particularly necessary in an industry such as ours where there has been considerable consolidation. Detailed information about these agreements, including a description of payout amounts under a hypothetical change-in-control or termination of the named executives as of the last business day of 2007, is included beginning at page 120.

Given the state of our industry and their unique positions with our Company, Messrs. Killinger and Rotella have employment agreements that provide benefits upon termination under certain circumstances before and after a change-in-control. Mr. Killinger's employment agreement was negotiated in 1998 when our Board of Directors determined that due to consolidations in the industry, change-in-control protection was appropriate for both our Company and Mr. Killinger. We believe Mr. Killinger's arrangement was consistent with market practices as they existed at that time and as are still common in both the financial services industry and among other large companies. Mr. Rotella's employment agreement, negotiated and signed in 2004, is similar to Mr. Killinger's arrangement. The Committee concluded that Mr. Rotella's employment agreement was necessary to attract and retain the caliber of executive talent found at his level. Messrs. Killinger's and Rotella's agreements were both designed to protect our Company's and the executive's interests, and to help us maintain a high level of stability within our executive ranks.

Each of the other named executives other than Ms. Chapman has our standard executive change-in-control agreement which provides benefits only upon a change-in-control. Ms. Chapman's change-in-control agreement was superseded by her severance agreement, discussed below. The change-in-control arrangements for other named executives are similar to those provided in the employment agreements for Messrs. Rotella and Killinger. The Committee believes that it is important for all top executives to have similar change-in-control protection to ensure the same level of focus and commitment during a potential change-in-control, without concern for their own financial situation and personal career opportunities should such an event occur.

Equity acceleration upon a change-in-control is a common practice within and outside the financial services industry. Equity compensation is an important tool in our compensation portfolio, and allowing vesting upon a change-in-control ensures that named executives' interests are aligned with those of our shareholders.

As described at page 120, the ETRIP has an acceleration feature upon a change-in-control, providing an additional three years of service credit and additional vesting credit. We designed the plan in this manner under the assumption that the executive would lose the ability to earn retirement credits under this plan if a change-in-control occurred.

#### *Executive Severance Plan*

In January 2008, the Committee approved the material terms of a severance plan for executive officers other than Mr. Killinger and Mr. Rotella, whose severance benefits are determined by their employment agreements. The new severance plan entitles each covered executive to a cash payment if we terminate his or her employment for any reason other than cause (as defined in the covered executive's existing change-in-control agreement) equal to 1.5 times the sum of (i) the executive's base salary plus (ii) the higher of (A) the executive's target bonus for the current year or (B) the executive's actual bonus for the prior year. No benefits under the severance plan will be paid to any covered executive who becomes entitled to benefits under his or her change-in-control agreement. The Committee took this action to promote retention of covered named executives and to provide them with severance protection at a standardized level. Messrs. Casey, Corcoran and Cathcart are included in

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the group of covered executives under the plan. Because she is no longer an executive officer, Ms. Chapman is not eligible for benefits under the plan.

### *Agreement with Fay L. Chapman*

We entered into a severance and mutual release agreement with Ms. Chapman, our former Chief Legal Officer, in connection with her upcoming retirement from the Company on June 30, 2008. Ms. Chapman ceased serving as Chief Legal Officer and an executive officer in December 2007. Under the severance agreement, we will pay Ms. Chapman a base salary through June 30, 2008 at the annualized rate of \$1,062,000. Effective July 1, 2008, we will enter into a two-year consulting arrangement with her under which we will pay her an aggregate of \$2,650,000. Under the severance agreement, the performance criteria associated with her 2005 and 2007 annual restricted stock grants were removed and we agreed to pay Ms. Chapman her full 2007 target bonus of \$310,000. We entered into the severance agreement in order (i) to ensure Ms. Chapman's availability to assist us in transitioning to an interim and permanent successor to her as Chief Legal Officer, (ii) to assist us with a number of significant litigation and other matters we currently face and others that may arise in the future, (iii) to acknowledge her long service to our Company which included over 10 years as a senior executive and a similar period of time before that representing us as outside counsel, and (iv) to assist Ms. Chapman in her transition to retirement.

### **Other Policies and Considerations**

#### *Executive Stock Ownership Guidelines*

We further align the interests of named executives and shareholders through executive stock ownership guidelines. The following table shows the guidelines applicable to each named executive, as a multiple of base salary. Ms. Chapman no longer is subject to the guidelines since she no longer is an executive officer.

<b>Named Executive</b>	<b>Stock Ownership Guideline</b>
Kerry K. Killinger	10x base salary
Thomas W. Casey	4x base salary
Stephen J. Rotella	4x base salary
James B. Corcoran	4x base salary
Ronald J. Cathcart	3x base salary
Fay L. Chapman	N/A

Named executives can use shares of unvested restricted stock to satisfy the guidelines, and can also use amounts deferred under the Deferred Compensation Plan to the extent that those balances are invested in the plan's earnings method based on our stock price. We give newly hired named executives a five-year period to satisfy the guidelines. All named executives have either exceeded their ownership requirements or are within the five-year period for satisfying them.

#### *Recovery of Equity Awards and Related Gains*

We maintain claw-back provisions within our standard form stock option and restricted stock award agreements for awards made in 2006 and beyond. These agreements also contain provisions assigning intellectual property rights to us. In accordance with these provisions, named executives who violate employee non-solicitation obligations will forfeit all of their outstanding equity awards whether or not they have vested, as of the date of the violation or the date of our discovery of the violation. In addition, the named executives would be required to forfeit any gains realized on our stock or options obtained under these awards if the gain is realized during the 12 months preceding the violation. We first implemented these provisions in 2006 to protect our intellectual property and human capital and

to help ensure that the named executives act in our best interests and the best interests of our shareholders.

*Tax and Accounting Effects*

We consider the tax and accounting treatment of the various components and levels of executive compensation. These considerations generally are not primary factors underlying compensation decisions; however, we balance primary compensation objectives with our desire to put the Company in the best possible position with respect to tax and accounting treatment. In particular, we generally pay compensation to named executives that is "performance-based" and therefore deductible under Section 162(m) of the Internal Revenue Code. For this reason, we have not increased Mr. Killinger's base salary since 1999. However, we will pay non-deductible compensation when appropriate to achieve our compensation objectives. We believe the stock options and performance shares we awarded in 2007 will qualify as performance-based compensation under Section 162(m).

**Report of the Human Resources Committee**

The Human Resources Committee has reviewed and discussed the Compensation Discussion and Analysis set forth above with Company management. Based on such review and discussions, the Human Resources Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this Proxy Statement.

HUMAN RESOURCES COMMITTEE

James H. Stever, Chair

Stephen E. Frank

Charles M. Lillis

Phillip D. Matthews

Margaret Osmer McQuade

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**2007 Summary Compensation Table**

The following table shows all 2007 compensation we paid to our Chief Executive Officer, Chief Financial Officer, three most highly paid persons serving as executive officers at the end of 2007 and one former executive officer, Fay L. Chapman, who is also included under SEC rules because she would have been among the three most highly paid other executive officers but for the fact that she ceased serving as an executive officer before December 31, 2007. All individuals listed in the following table are referred to in this Proxy Statement as the "named executives." Annual Compensation includes amounts deferred at the named executive's election. The following table also includes 2006 compensation for Messrs. Killinger, Casey, Rotella and Corcoran, but does not include 2006 compensation for Mr. Cathcart or Ms. Chapman in accordance with SEC guidance because they were not named executives in 2006.

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity Incentive Plan Compensation (\$)	Change in Pension Value and Nonqual. Deferred Comp. Earnings (\$)	All Other Compensation (\$)	Total (\$)
Kerry K. Killinger Chairman and Chief Executive Officer	2007	1,000,000		669,104	3,183,914			397,752	5,250,770
	2006	1,000,000		2,251,139	5,148,464	4,074,000	1,270,684	501,572	14,245,859
Thomas W. Casey Executive Vice President and Chief Financial Officer	2007	672,000		189,338	958,902	391,200	130,053	99,153	2,440,646
	2006	620,000		878,838	1,517,087	1,356,060	97,613	95,983	4,565,581
Stephen J. Rotella President and Chief Operating Officer	2007	922,000		(354,332)	2,020,610	912,800	262,861	162,592	3,926,531
	2006	900,000		2,126,040	1,514,458	3,142,800	639,692	130,004	8,452,994
James B. Corcoran Executive Vice President and President, Retail Banking	2007	622,000		402,038	365,988	277,100	158,565	756,816	2,582,506
	2006	345,769	1,500,000	136,183	135,691	931,200	149,174	102,483	3,300,500
Ronald J. Cathcart Executive Vice President and Chief Enterprise Risk Officer	2007	592,000		389,124	451,971	153,220	107,623	268,046	1,961,984
Fay L. Chapman Former Senior Executive Vice President and Chief Legal Officer	2007	752,000	310,000	1,174,079	719,249		379,484	61,572	3,086,384

**Salary**

The Human Resources Committee established 2007 base salaries for our named executives in January 2007. As discussed above, Mr. Killinger did not receive a base salary increase in 2007 in order to maintain the tax deductibility of the full amount of his salary under Section 162(m) of the Internal Revenue Code. All other named executives received base salary increases of \$22,000 to replace the value of Company-paid perquisites which we no longer provided as of January 1, 2007. In addition, Mr. Casey and Ms. Chapman received 2007 base salary increases of 4.8% and 4.2%, respectively, in recognition of the increasing complexity of each executive's role. Mr. Corcoran joined our Company in May 2006, so the 2006 salary reported for him represents only a partial year.

**Bonus**

Under the terms of our severance agreement with Ms. Chapman, discussed at page 101 above, we waived Company performance criteria applicable to her 2007 bonus payout under the Leadership Bonus Plan. As a result, she received 100% of her target bonus payout for 2007. Because the performance criteria were waived, we report this amount in the table as "Bonus" rather than

"Non-Equity Incentive Plan Compensation". The 2006 amount shown for Mr. Corcoran was a cash signing bonus we paid him upon hire.

### **Stock Awards and Option Awards**

These columns reflect the dollar amount recognized for financial statement reporting purposes, in accordance with applicable SEC rules and guidance and FAS 123R, for shares of unvested restricted stock and outstanding performance share awards and for stock options held by the named executives, which may include amounts from awards made in and prior to the years shown. The fair value of our restricted stock is based on the market value of our common stock on the applicable measurement date for accounting purposes. For additional information on the valuation of our 2007 restricted stock and performance share awards, and regarding significant factors, assumptions and methodologies used in determining the fair value of our stock options, see Note 21 to the Washington Mutual, Inc. and Subsidiaries Consolidated Financial Statements contained in the Company's Form 10-K for the year-ended December 31, 2007, as supplemented for stock options by the table at page 107. Any amounts realized by the named executives on stock option awards will depend upon whether the options vest and our stock price at the time of exercise.

Amounts shown in the Stock Awards column for Messrs. Killinger, Casey and Rotella include the effects of reversals of previously recorded expenses in the amounts of \$2,121,214, \$521,964 and \$1,276,130, respectively, reported as 2006 compensation in the Summary Compensation Table included in our definitive proxy statement filed with the SEC on March 19, 2007. The expenses were reversed because vesting of prior restricted stock and performance share awards was conditioned on achieving certain corporate performance criteria which we did not fully achieve. In accordance with SEC guidance, we did not include the effects of expense reversals for Mr. Cathcart or Ms. Chapman because the previous expense was not reported in a prior year's Summary Compensation Table.

### **Non-Equity Incentive Plan Compensation**

This column represents the cash bonuses paid to the named executives for 2007 performance pursuant to our Leadership Bonus Plan. Mr. Killinger did not accept a bonus for 2007.

### **Change in Pension Value and Nonqualified Deferred Compensation Earnings**

As indicated in the following table, this column represents: (i) the actuarial increase or decrease in the present value of the named executives' benefits under the WaMu Pension Plan and the ETRIP determined using interest rate and mortality rate assumptions consistent with those used in our financial statements; and (ii) above-market interest for 2007 on balances in our Deferred Compensation Plan and Mr. Killinger's and Ms. Chapman's SERAP benefit. In accordance with applicable SEC regulations, interest is above market if it is paid at a rate that exceeds the Benchmark Rate, which is 120% of the applicable federal long-term rate. The annual interest rate we paid under these plans, including the Deferred Compensation Plan's interest method of earnings, was 5.83%, which in each case was lower than the Benchmark Rate of 6.27%. During 2007, the Deferred Compensation Plan's earnings rate for the interest method of earnings and the interest rate paid under the SERAP was based on a rate comparable to our unsecured junior debt with a ten-year maturity. The present value of Mr. Killinger's benefits under the ETRIP decreased due to a significant decrease in his average earnings used to calculate his ETRIP benefit. In accordance with SEC guidance, although the value for

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Mr. Killinger is a negative number, we included zero in this column of the Summary Compensation Table and for purposes of calculating Mr. Killinger's total compensation as reported in the table.

Name	WaMu Pension Plan Actuarial Increase (\$)	ETRIP Actuarial Increase/Decrease (\$)	Deferred Compensation Plan Above-Market Interest (\$)	SERAP Above-Market Interest (\$)	Total (\$)
Kerry K. Killinger	33,841	(749,170)			(715,329)
Thomas W. Casey	8,498	121,555			130,053
Stephen J. Rotella	8,925	253,936			262,861
James B. Corcoran	8,169	150,396			158,565
Ronald J. Cathcart	8,591	99,032			107,623
Fay L. Chapman	14,763	364,721			379,484

**All Other Compensation**

The amount of 2007 All Other Compensation reported for each named executive in the Summary Compensation Table above consisted of the following:

Name	Perquisites and Other Personal Benefits (\$) <sup>(1)</sup>	Relocation (\$) <sup>(2)</sup>	Tax Payments (\$) <sup>(3)</sup>	Company Credits to SERP (\$) <sup>(4)</sup>	Other (\$) <sup>(5)</sup>	Total (\$)
Kerry K. Killinger			832	387,920	9,000	397,752
Thomas W. Casey				90,153	9,000	99,153
Stephen J. Rotella				153,592	9,000	162,592
James B. Corcoran		493,070	251,306	3,440	9,000	756,816
Ronald J. Cathcart		221,842	1,572	35,632	9,000	268,046
Fay L. Chapman				52,572	9,000	61,572

(1) We eliminated Company-paid perquisites and personal benefits as of January 1, 2007. As a result, no named executive had any perquisites or personal benefits in 2007 in an amount required to be reported under SEC rules. Mr. Killinger continues to have access to Company aircraft for personal use but reimbursed the Company for our aggregate incremental cost related to his personal use in 2007.

(2) The amounts in this column represent Company-paid moving and relocation expenses. This includes our direct payment of costs incurred for travel, temporary housing and shipment of household goods. We paid these amounts under our management-level relocation plan and related procedures.

(3) The amount in this column for Mr. Killinger represents our payment of his tax liability for the value of gifts received by attendees, including Mr. Killinger and his spouse, of an employee recognition event we held in 2007. The amount in this column for Mr. Corcoran represents Company payments for taxes related to the relocation expenses disclosed in the table. The amount in this column for Mr. Cathcart represents our payment of tax liabilities related to his receipt of gifts at the same employee recognition event as Mr. Killinger, and related to the relocation expenses disclosed in the table. The tax payments related to relocation expenses differed significantly for Mr. Corcoran as compared to Mr. Cathcart because all of the relocation expenses shown in the table for Mr. Corcoran were taxable to him, but almost none of the relocation expenses shown for Mr. Cathcart were taxable to him.

(4) The amounts in this column represent amounts credited to the accounts of each named executive during 2007 under the SERP. This plan is described beginning at page 120.

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(5)

The amounts in this column represent the Company's matching contributions under the WaMu Savings (401(k)) Plan.

### Grants of Plan-Based Awards in 2007

The table below shows all plan-based awards we granted to named executives during 2007.

Name	HR Committee Approval Date	Grant Date	Estimated Possible Payouts Under Non-Equity Incentive Plan Awards			Estimated Future Payouts Under Equity Incentive Plan Awards			All Other Option Awards: Numbers of Securities Underlying Options (#)	Exercise or Base Price of Option Awards (\$/Sh.)	Grant Date Fair Value of Stock and Option Awards (\$)	
			Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (#)	Target (#)	Maximum (#)				
Kerry K. Killinger	1/16/07	1/19/07	0	3,650,000	5,475,000	23,400	93,600	234,000	355,800	44.67	4,148,352	
	1/16/07	1/19/07									133,700	5,972,379
	1/16/07	1/19/07										2,846,400
Thomas W. Casey	1/16/07	1/19/07	0	1,200,000	1,800,000	8,125	32,500	81,250	123,800	44.67	1,440,400	
	1/16/07	1/19/07									46,500	2,077,155
	1/16/07	1/19/07										990,400
Stephen J. Rotella	1/16/07	1/19/07	0	2,800,000	4,200,000	12,200	48,800	122,000	185,600	44.67	2,162,816	
	1/16/07	1/19/07									69,800	3,117,966
	1/16/07	1/19/07										1,484,800
James B. Corcoran	1/16/07	1/19/07	0	850,000	1,275,000	3,050	12,200	30,500	46,400	44.67	540,704	
	1/16/07	1/19/07									17,400	777,258
	1/16/07	1/19/07										371,200
Ronald J. Cathcart	1/16/07	1/19/07	0	470,000	705,000	3,550	14,200	35,500	75,800	44.67	629,344	
	1/16/07	1/19/07									15,800	705,786
	1/16/07	1/19/07										606,400
Fay L. Chapman	1/16/07	1/19/07	0	310,000	465,000	2,850	11,400	28,500	43,300	44.67	505,248	
	1/16/07	1/19/07									16,300	728,121
	1/16/07	1/19/07										346,400

The plan-based awards compensation reported in the Summary Compensation Table and the Grants of Plan-Based Awards Table above consisted of the following types of awards. For additional information on each type of award described below, see the "Annual Incentive Bonus" and "Long-Term Equity Incentive Compensation" sections of the Compensation Discussion and Analysis beginning at page 89.

### Non-Equity Incentive Plan Compensation

Non-Equity Incentive Plan Compensation amounts represent the threshold (0%), target (100%) and maximum (150%) amounts of cash bonuses that were payable to our named executives for 2007 performance under our Leadership Bonus Plan. The 2007 Leadership Bonus Plan is discussed and analyzed beginning at page 89. We paid awards for 2007 performance in January 2008 at 32.6% of the target amounts reported in the table, other than for Mr. Killinger, who did not accept a bonus, and Ms. Chapman, who received 100% of her target bonus under the terms of her severance agreement described at page 101. The cash payout for each other named executive based on this percentage is reported in the Non-Equity Incentive Plan Compensation column of the Summary Compensation Table at page 103.

### Estimated Future Payouts Under Equity Incentive Plan Awards

The awards reported in these columns with threshold (25%), target (100%) and maximum (250%) number of shares of our common stock represent shares that potentially may be issued as future payouts for the performance share awards made to the named executives as part of our 2007 annual equity awards in January 2007 for the 2007-2009 performance cycle. Performance share awards are discussed and analyzed beginning at page 94. Performance share awards are contingent performance

awards paid out, in either cash or shares of our common stock at our discretion, at the end of a three-year period only to the extent of our achievement of specified performance measures. There is no payout if our performance is below the 30th percentile of peer group companies. Performance share awards earn dividend equivalents that are accrued in the form of additional performance shares paid in our common stock, or cash at our election, when and to the extent the related performance shares are paid.

The awards reported with only a maximum number of shares represent annual restricted stock awards granted to the named executives in January 2007 under our Amended and Restated 2003 Equity Incentive Plan as part of our annual equity awards. The general terms of our annual restricted stock awards are discussed and analyzed beginning at page 94. As discussed at page 94, for all named executives other than Ms. Chapman, only 32.6% of these shares are eligible to vest over the three-year vesting schedule due to our results under the 2007 Leadership Bonus Plan performance measures. 100% of the shares we granted to Ms. Chapman are eligible to vest under the terms of our severance agreement with her.

### All Other Option Awards

The amounts reported in this column represent annual stock option grants made to the named executives in January 2007 as part of our annual equity awards. The grant date differs from the approval date reported in the table because we grant annual stock options on the second business day after the public release of our year-end financial results. We granted the awards under our Amended and Restated 2003 Equity Incentive Plan, which expressly prohibits re-pricing of stock options without shareholder approval. Stock options generally expire ten years after the grant date. The expiration period is accelerated if the holder's employment with us terminates under certain circumstances.

### Option Awards FAS 123R Valuation

The Option Awards column in the Summary Compensation Table at page 103 includes expense related to stock option awards granted to the named executives on the following dates: January 21, 2005; December 15, 2005, January 20, 2006; June 15, 2006 and January 19, 2007. The Option Awards column in the Director Compensation Table at page 136 includes expense related to stock option awards granted to non-employee directors on January 20, 2006 and January 19, 2007. The significant factors and assumptions used in determining the fair value of these stock options is reported in the following table:

Significant Factors and Assumptions	Options Granted to Non-Employee Directors and Messrs. Killinger, Casey Rotella and Ms. Chapman on 1/21/05	Options Granted to Mr. Cathcart on 12/15/05	Options Granted to Non-Employee Directors and to Messrs. Killinger, Casey and Rotella and Ms. Chapman on 1/20/06	Options Granted to Mr. Corcoran on 6/15/06	Options Granted to all Named Executives and Non-Employee Directors on 1/19/07
Grant Date Fair Value(\$)	10.71	11.16	8.68	8.96	8.00
Dividend Yield(%)	4.20	4.15	4.70	4.70	4.70
Expected Volatility(%)	31.00	29.08	25.50	24.80	21.90
Risk Free Interest Rate(%)	3.84	4.41	4.28	5.02	4.72
Expected Life (in Years)	7.0	7.0	6.2	6.2	6.3



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Outstanding Equity Awards at the End of 2007

This table shows the equity awards that have been previously awarded to each of the named executives and which remained outstanding as of December 31, 2007.

Name	Option Awards <sup>(1)</sup>				Stock Awards			
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested (\$) <sup>(12)</sup>	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#) <sup>(13)</sup>	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$) <sup>(14)</sup>
Kerry K. Killinger	580,442		21.92	12/15/08	65,534 <sup>(7)</sup>	891,918	249,612	3,397,213
	774,105		16.96	12/21/09				
	795,001		33.42	12/19/10				
	1,200,000		30.79	12/18/11				
	900,000		36.53	12/17/12				
	760,000		39.53	12/16/13				
	178,666	89,334 <sup>(2)</sup>	42.17	1/21/15				
	152,966	305,934 <sup>(3)</sup>	43.33	1/20/16				
	355,800 <sup>(4)</sup>	44.67	1/19/17					
Thomas W. Casey	147,171		35.34	10/22/12	28,600 <sup>(7)</sup>	389,246	99,382	1,352,584
	147,263		36.53	12/17/12				
	230,000		39.53	12/16/13				
	60,599	30,301 <sup>(2)</sup>	42.17	1/21/15				
	37,033	74,067 <sup>(3)</sup>	43.33	1/20/16				
		123,800 <sup>(4)</sup>	44.67	1/19/17				
Stephen J. Rotella	163,666	81,834 <sup>(2)</sup>	42.17	1/21/15	97,844 <sup>(8)</sup>	1,331,652	131,771	1,793,407
	77,766	155,534 <sup>(3)</sup>	43.33	1/20/16				
		185,600 <sup>(4)</sup>	44.67	1/19/17				
James B. Corcoran	27,777	55,556 <sup>(5)</sup>	43.67	6/15/16	12,550 <sup>(9)</sup>	170,804	9,120	124,127
		46,400 <sup>(4)</sup>	44.67	1/19/17				
Ronald J Cathcart	46,666	23,334 <sup>(6)</sup>	44.18	12/15/15	6,344 <sup>(10)</sup>	86,340	30,693	417,735
		75,800 <sup>(4)</sup>	44.67	1/19/17				
Fay L. Chapman	117,008		33.42	12/19/10	33,643 <sup>(11)</sup>	457,886	42,721	581,439
	130,000		36.53	12/17/12				
	95,000		39.53	12/16/13				
	24,999	12,501 <sup>(2)</sup>	42.17	1/21/15				
	12,966	25,934 <sup>(3)</sup>	43.33	1/20/16				
		43,300 <sup>(4)</sup>	44.67	1/19/17				

(1) All option amounts in this table have been adjusted to reflect past stock-splits.

(2) These options were granted on January 21, 2005 and vest in one-third increments on each of the first three anniversaries of the date of grant.

(3) These options were granted on January 20, 2006 and vest in one-third increments on each of the first three anniversaries of the date of grant.

(4)

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These options were granted on January 19, 2007 and vest in one-third increments on each of the first three anniversaries of the date of grant.

(5)

This option was granted on June 15, 2006 and vests in one-third increments on each of the first three anniversaries of the date of grant.

(6)

This option was granted on December 15, 2005 and vests in one-third increments on each of the first three anniversaries of the date of grant.

(7)

These shares were issued on January 20, 2006 and vest in one-third increments on each of the first three anniversaries of the date of issuance.

(8)

33,334 of these shares were issued on January 20, 2006 and vest in one-third increments on each of the first three anniversaries of the date of issuance. 64,510 of these shares were issued on January 10, 2005 and vest on January 31, 2010.

(9)

These shares were issued on June 15, 2006 and vest in one-third increments (including accrued dividend shares) on each of the first three anniversaries of the date of issuance.

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(10) These shares were issued on December 15, 2005 and vest in one-third increments (including accrued dividend shares) on each of the first three anniversaries of the date of issuance.

(11) 6,200 of these shares were issued on January 28, 2005 and vested on January 28, 2008; 10,000 and 17,443 of these shares were issued on January 20, 2006 and January 19, 2007, respectively, and vest in each case in one-third increments on each of the first three anniversaries of the date of issuance.

(12) The values contained in this column were calculated by multiplying the number of shares by \$13.61, which was the closing price of our common stock reported on the NYSE on December 31, 2007.

(13) This column includes: (i) the threshold amounts of 5-year performance restricted stock (referred to as "5-Year RS" in the table below) and all accrued dividend shares through the end of 2007; (ii) the threshold amounts of performance share awards (referred to as "PSAs" below) for the 2005-2007, 2006-2008 and 2007-2009 performance cycles; (iii) unvested shares from the 2005 annual restricted stock award (referred to as "2005 RS" below) that were eligible to vest as of December 31, 2007 based on our performance under applicable performance criteria; and (iv) unvested shares from the 2007 annual restricted stock award (referred to as "2007 RS" below) that are eligible to vest based on our performance under applicable performance criteria, as discussed at page 94. Under the terms of her severance agreement discussed at page 101, the remaining performance criteria for the 2005 RS and 2007 RS awards were waived for Ms. Chapman, and those shares are reported with other non-performance based stock awards. The restricted stock and performance share awards reported in this column vest to the extent of our achievement of applicable performance measures on the applicable dates in the following table. The performance criteria for the 2007 RS, PSAs and 5-Year RS are discussed beginning at page 94.

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Performance Share Awards and Performance Restricted Stock Vesting Terms

Name	Type of Award	Reported Amount	Shares or Awards not Vested	Vesting Dates
Kerry K. Killinger	2005-2007 PSA	Threshold	24,250	Pays out in 2008 depending on Company performance after 2005-2007 results are compared with peers. The payout amount was zero.
	2006-2008 PSA	Threshold	23,100	Pays out in 2009 depending on Company performance after 2006-2008 results are compared with peers.
	2007-2009 PSA	Threshold	23,400	Pays out in 2010 depending on Company performance after 2007-2009 results are compared with peers.
	5-Year RS	Threshold	87,968	Vest after the performance period ends on December 31, 2009 to the extent of the Company's achievement of specified performance measures.
	2005 RS	Target	44,250	Remaining unvested shares were eligible to vest on January 28, 2008 to the extent of our achievement of specified performance measures. We did not meet the performance criteria, thus the payout amount was zero.
	2007 RS	Target	46,644	These shares are eligible to vest in equal annual installments on January 18, 2008, January 19, 2009 and January 19, 2010.
Thomas W. Casey	2005-2007 PSA	Threshold	8,225	Pays out in 2008 depending on Company performance after 2005-2007 results are compared with peers. The payout amount was zero.
	2006-2008 PSA	Threshold	7,825	Pays out in 2009 depending on Company performance after 2006-2008 results are compared with peers.
	2007-2009 PSA	Threshold	8,125	Pays out in 2010 depending on Company performance after 2007-2009 results are compared with peers.

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	5-Year RS	Threshold	43,984	Vest after the performance period ends on December 31, 2009 to the extent of the Company's achievement of specified performance measures
	2005 RS	Target	15,000	Remaining unvested shares were eligible to vest on January 28, 2008 to the extent of our achievement of specified performance measures. We did not meet the performance criteria, thus the payout amount was zero.
	2007 RS	Threshold	16,222	These shares are eligible to vest in equal annual installments on January 18, 2008, January 19, 2009 and January 19, 2010.
Stephen J. Rotella	2005-2007 PSA	Threshold	12,325	Pays out in 2008 depending on Company performance after 2005-2007 results are compared with peers. The payout amount was zero.
	2006-2008 PSA	Threshold	11,750	Pays out in 2009 depending on Company performance after 2006-2008 results are compared with peers.
	2007-2009 PSA	Threshold	12,200	Pays out in 2010 depending on Company performance after 2007-2009 results are compared with peers.
	5-Year RS	Threshold	58,645	Vest after the performance period ends on December 31, 2009 to the extent of the Company's achievement of specified performance measures.
	2005 RS	Target	12,500	Remaining unvested shares were eligible to vest on January 28, 2008 to the extent of our achievement of specified performance measures. We did not meet the performance criteria, thus the payout amount was zero.
	2007 RS	Threshold	24,351	These shares are eligible to vest in equal annual installments on January 18, 2008, January 19, 2009 and January 19, 2010.
James B. Corcoran	2007-2009 PSA	Threshold	3,050	Pays out in 2010 depending on Company performance after 2007-2009 results are compared with peers.

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	2007 RS	Threshold	6,070	These shares are eligible to vest in equal annual installments on January 18, 2008, January 19, 2009 and January 19, 2010.
Ronald J. Cathcart	2006-2008	Threshold	2,600	Pays out in 2009 depending on Company performance after 2006-2008 results are compared with peers.
	2007-2009	Threshold	3,550	Pays out in 2010 depending on Company performance after 2007-2009 results are compared with peers.
	5-Year RS	Threshold	19,031	Vest after the performance period ends on December 31, 2009 to the extent of the Company's achievement of specified performance measures
	2007 RS	Target	5,512	These shares are eligible to vest in equal annual installments on January 18, 2008, January 19, 2009 and January 19, 2010.
Fay L. Chapman	2005-2007	Threshold	3,400	Pays out in 2008 depending on Company performance after 2005-2007 results are compared with peers. The payout amount was zero.
	2006-2008	Threshold	2,750	Pays out in 2009 depending on Company performance after 2006-2008 results are compared with peers.
	2007-2009	Threshold	2,850	Pays out in 2010 depending on Company performance after 2007-2009 results are compared with peers.
	5-Year RS	Threshold	33,721	Vest after the performance period ends on December 31, 2009 to the extent of the Company's achievement of specified performance measures

(14)

The values contained in this column were calculated by multiplying the number of shares by \$13.61, which was the closing price of our common stock reported on the NYSE on December 31, 2007.

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**Exercised Options and Vested Restricted Stock in 2007**

This table shows the stock options that were exercised by, and the restricted stock that vested for, each named executive during 2007.

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#) <sup>(1)</sup>	Value Realized on Exercise (\$) <sup>(2)</sup>	Number of Shares Acquired on Vesting (#) <sup>(3)</sup>	Value Realized on Vesting(\$) <sup>(7)</sup>
Kerry K. Killinger			44,250	2,004,968
			32,766	1,463,657
Thomas W. Casey	943	7,855	15,000	679,650
	1,825	13,031	3,418 <sup>(4)</sup>	138,014
			14,300	638,781
Stephen J. Rotella			12,500	566,375
			16,666	744,470
James B. Corcoran			6,009 <sup>(5)</sup>	258,821
Ronald J. Cathcart			6,344 <sup>(6)</sup>	96,110
Fay L. Chapman			5,000	223,350
			6,200	280,922

(1) Mr. Casey exercised two stock options during 2007, both of which were granted in 2002.

(2) In accordance with applicable rules, the amount reported in this column is calculated by determining the difference between (i) the aggregate market price of the underlying shares on the date of exercise of the option and (ii) the aggregate exercise price for the exercised options. In calculating aggregate market price of the underlying shares on the date of exercise, we used the closing price of one share of our common stock, as reported on the NYSE on the applicable date of the exercise of the option.

(3) This column represents the number of shares of restricted stock that vested for each named executive during 2007. Upon vesting, the transfer restrictions associated with restricted stock lapse. For Messrs. Killinger, Casey and Rotella and Ms. Chapman, the shares in this column include one-third of the shares granted to each of them as part of their 2005 and 2006 annual equity awards.

(4) These shares were part of Mr. Casey's sign-on equity award, including accrued dividends, made when he joined our Company in 2002.

(5) These shares were part of Mr. Corcoran's sign-on equity award, including dividends, made when he joined our Company in 2006.

(6) These shares were part of Mr. Cathcart's sign-on equity award, including dividends, made when he joined our Company in 2005.

(7) In accordance with applicable rules, the amounts reported in this column were calculated by multiplying the number of shares that vested during 2007 for each named executive by the closing price of one share of our common stock, as reported on the NYSE on the applicable date of vesting.

**2007 Pension Benefits**

The table below shows the present value of accumulated benefits payable to each of the named executives, including the number of years of service credited to each such named executive, under the WaMu Pension Plan and Executive Target Retirement Income Plan ("ETRIP") determined using interest rate and mortality rate assumptions consistent with those used in our financial statements. None of the benefits reported in the table below was paid in 2007.

<b>Named Executive</b>	<b>Plan Name</b>	<b>Years of Credited Service (#)<sup>(1)</sup></b>	<b>Present Value of Accumulated Benefits (\$) <sup>(2)</sup></b>
Kerry K. Killinger	WaMu Pension Plan	32.00	321,448
	ETRIP	13.00	3,155,473 <sup>(3)</sup>
Thomas W. Casey	WaMu Pension Plan	5.00	32,093
	ETRIP	5.25	474,078 <sup>(3)</sup>
Stephen J. Rotella	WaMu Pension Plan	3.00	17,141
	ETRIP	3.00	1,474,810 <sup>(3)</sup>
James B. Corcoran	WaMu Pension Plan	2.00	8,169
	ETRIP	1.67	299,570 <sup>(3)</sup>
Ronald J. Cathcart	WaMu Pension Plan	2.00	8,591
	ETRIP	2.08	244,763 <sup>(3)</sup>
Fay L. Chapman	WaMu Pension Plan	10.00	77,312
	ETRIP	10.33	1,651,212 <sup>(3)</sup>

(1) The ETRIP credits years of executive service only beginning with 1995.

(2) In accordance with applicable SEC rules, dollar amounts in this column were computed on December 31, 2007, which was the WaMu Pension Plan measurement date used for financial statement reporting purposes with respect to our audited financial statements for 2007. For purposes of this table, we assume a retirement age of 65, the normal retirement age in the WaMu Pension Plan. Furthermore, we assume a benefit payment date for the ETRIP that is the earlier of age 62 and 5 years of executive service or age 65. Further information on how these amounts were calculated is given in the narrative below.

(3) The named executives were vested in the ETRIP as of the end of 2007 in the following amounts: Mr. Killinger: 80%, Mr. Casey: 80%, Mr. Rotella: 40%, Mr. Corcoran: 20%, Mr. Cathcart: 40%, and Ms. Chapman: 80%. Had the named executives been terminated on December 31, 2007 for any reason other than cause, as defined in the plan, the ETRIP benefits for each named executive as of such date would have been as follows: Mr. Killinger: \$4,163,078, Mr. Casey: \$1,293,336, Mr. Rotella: \$959,290, Mr. Corcoran: \$103,497, Mr. Cathcart: \$159,719, and Ms. Chapman: \$1,423,695. The ETRIP generally defines "cause" for this purpose as fraud, embezzlement, theft or any other crime of moral turpitude or dishonesty in the executive's relationship with the Company (without necessity of formal criminal proceedings being initiated).

**Cash Balance Pension Plan**

Our cash balance defined benefit plan, the WaMu Pension Plan, provides that participants receive benefit credit accruals as a percentage of eligible compensation and interest accruals on current and prior benefit accruals. The current benefit accrual rate is based on years of service as follows:

for benefit service less than five years, the benefit credit is 4.0%;



for benefit service from five to less than ten years, the benefit credit is 5.0%;

for benefit service from ten to less than fifteen years, the benefit credit is 6.0%;

for benefit service from fifteen to less than twenty years, the benefit credit is 7.0%; and

for twenty years or more of benefit service, the benefit credit is 8.0%.

Eligible compensation includes base salary, cash incentive payments, bonuses and overtime, up to the annual compensation limitation contained in Section 401(a)(17) of the Internal Revenue Code of 1986, as amended (the "Code"), and less any deferrals by the executive into our Deferred Compensation Plan. The WaMu Pension Plan credits interest on all cash balance benefit accruals at the annual rate quoted at the beginning of each year for the average annual yield on U.S. government securities of a constant maturity of 30 years for all business days during the prior November. The Pension Plan credits benefit accruals each pay period and interest on a daily basis, and the annual interest credit rate for 2007 was 4.69%.

In general, all employees, including the named executives, become eligible to participate in the WaMu Pension Plan beginning with the quarter following completion of one year of service with the Company during which they work a minimum of 1,000 hours. An employee's cash balance in the WaMu Pension Plan becomes vested at a graduated rate after two years of service, with full vesting after five years of active service, except that eligible employees who first began employment after December 31, 2005, vest after five years of service with no graduated vesting. Employees accruing at least one hour of service after December 31, 2007 will be 100% vested after three years of service. There are no employee contributions to the WaMu Pension Plan.

Upon termination, participants may elect to receive a lump sum distribution of their vested cash balances or an annuitized payment from the WaMu Pension Plan's trust fund. The WaMu Pension Plan is designed to comply with the Employee Retirement Income Security Act of 1974, as amended (ERISA).

The WaMu Pension Plan Present Value of Accumulated Benefits reported in the table above was calculated as follows: for each named executive, the cash balance benefit as of December 31, 2007 was projected to age 65 using an assumed long-term interest crediting rate of 5.40% with no probability of death assumed before age 65. The present value of this projected benefit is established using the same demographic and economic assumptions we used in our audited financial statements contained in our Annual Report on Form 10-K for the year ended December 31, 2007. The present value is then discounted back to December 31, 2007, using the financial statement discount rate assumption of 6.40% with no probability of death assumed before age 65.

#### **Executive Target Retirement Income Plan**

In 2004 we established the ETRIP to provide retirement benefits for our executive officers, including the named executives. The ETRIP replaced the Supplemental Executive Retirement Accumulation Plan (the "SERAP"), discussed below, for our executive officers. The ETRIP was designed to provide a market competitive retirement benefit for participants. The ETRIP provides supplemental retirement benefits that, as a lump sum, are equal to 6.5 times a participant's average base salary and bonus during the last five calendar years (excluding compensation for years during which the participant was ineligible under the plan), reduced proportionally for executive service of less than 25 years. For this purpose, only executive service beginning with 1995 and beyond is considered. This benefit is offset by a participant's vested balances in our Supplemental Employees' Retirement Plan (the "SERP"), the SERAP, the WaMu Pension Plan, and our contributions for that employee to our 401(k) plan. Benefits under the ETRIP vest in 20% increments over five years, counting only full years of executive service on or after January 1, 2004. Upon a change-in-control of the Company, each participant would receive an additional three years of service credit, depending on the participant's

existing change-in-control or employment agreement with us. In addition, our or a successor company's ability to amend the ETRIP after a change-in-control is strictly prohibited, except to provide for additional offsets for any retirement plans adopted after a change-in-control. In compliance with Section 409A of the Code, six months after termination of employment, each participant receives a lump sum payment equal to his or her balance, except that any participant may make an irrevocable election at least one year before the distribution to receive annual installments over a period of up to 20 years so long as the participant's plan balance exceeds \$500,000 at the time of termination. Anyone who does not make an election will receive a lump sum payment at least six months after termination of employment.

The ETRIP Present Value of Accumulated Benefits reported in the table above is calculated as follows:

For each named executive, the average base salary and bonus during the last five calendar years with our Company (excluding compensation for years during which the named executive was ineligible under the plan) is multiplied by 6.5 and is designated the "target benefit."

This target benefit is multiplied by the months of executive service (capped at 300) with a full month credited in the first month as a Company executive, regardless of the actual day within the first month of the executive designation, and then divided by 300. For example, an executive who has been with us for two years would receive 24 months of executive service, which means that he or she would have 8% of the total executive service possible under the plan.

This lump sum benefit is assumed payable at the earlier of age 62 with 60 months of executive service, or age 65.

The vesting schedule of 20% per projected completed year of executive service at the benefit payment date is then applied and this final amount is the maximum lump sum that is payable from the ETRIP.

***Offsets to the Maximum Lump Sum Payable under the Executive Target Retirement Income Plan***

Once the maximum lump sum is determined, offsets are calculated, and the ETRIP benefit is reduced by the amount of our contributions or credits to our other retirement plans, as described below. The ETRIP amounts reported in the table above reflect applicable offsets pursuant to the plan. As offsets, the following amounts are subtracted from the maximum ETRIP amount as calculated above:

As applicable, each named executive's Company-provided benefit (including earnings thereon) in the WaMu Savings Plan as of December 31, 2007, projected to the assumed benefit payment date at a compound per annum rate of 7%.

As applicable, each named executive's benefit in the WaMu Pension Plan as of December 31, 2007, projected to the assumed benefit payment date at a compound per annum rate of 4.70%.

As applicable, each named executive's benefit in the SERP as of December 31, 2007, projected to the assumed benefit payment date at a compound per annum rate of 4.70%.

As applicable, each named executive's benefit in the SERAP as of December 31, 2007, projected to the assumed benefit payment date at a compound per annum rate of 5.48%.

For each named executive, the remaining ETRIP benefit after subtracting each applicable component described above is discounted back from the assumed payment date to December 31, 2007, using the same 5.70% discount rate contained in our 2007 financial statements and ignoring mortality before the assumed payment date.

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Amounts shown in the "Present Value of Accumulated Benefits" column in the table above are the actuarial present values of the December 31, 2007 accumulated benefits. These amounts do not correspond to actual amounts that would have been payable upon termination on December 31, 2007. For information on amounts payable to the named executives under the ETRIP upon termination on December 31, 2007, see footnote 3 to the Pension Benefits Table at page 114 above.

As discussed above, in January 2008 the Human Resources Committee approved amendments to the ETRIP to exclude from participation new named executives hired or otherwise made eligible after January 1, 2008. The Committee approved an amendment to the plan providing that, effective December 31, 2012, participants will cease to accrue employment service credits for benefits and vesting purposes, except in the case of a change-in-control, in which case participants would continue to receive an additional three years of service credit. In connection with this amendment, the Committee also approved other amendments affecting the benefit calculation formula. Effective December 31, 2012, benefits for each participant no longer will be reduced by (i) Company contributions or credits the participant receives under our other general and executive retirement benefit plans and the WaMu Savings Plan, or (ii) the effects of decreases in base salary and bonus during the five-year measurement period.

**2007 Nonqualified Deferred Compensation**

We offer two nonqualified defined contribution plans the Deferred Compensation Plan and the SERP to the named executives. Both of these plans are described in detail below. In addition, certain highly compensated employees, not including the named executives or other executive officers, participate in the SERAP. Before our adoption of the ETRIP in 2004, some of our executive officers, including the named executives, were eligible to receive benefit accruals in the SERAP based on age and service requirements then in effect under the plan. Mr. Killinger and Ms. Chapman are the only named executives who have an existing SERAP account benefit, which continues to receive interest credits but not further benefit accruals. No other named executive had any SERAP benefit when the executive officer benefit accruals ended in 2004. Mr. Casey elected to receive the withdrawal shown in the table below from the Deferred Compensation Plan at the time of his initial deferral election.

Name	Executive Contributions in 2007 (\$) <sup>(1)</sup>	Company Contributions in 2007 (\$) <sup>(2)</sup>	Aggregate Earnings in 2007 (\$)	Aggregate Withdrawals/ Distributions in 2007 (\$)	Aggregate Balance at December 31, 2007 (\$)
Kerry K. Killinger			(14,610,150) <sup>(3)</sup>		8,027,887
Deferred Compensation Plan		387,920	159,766		3,692,362 <sup>(5)</sup>
SERP			156,953 <sup>(4)</sup>		2,778,654
SERAP			15,866		352,170
Deferred Bonus Arrangement					
Thomas W. Casey	620,449		(419,776)	178,479	3,125,793
Deferred Compensation Plan		90,153	9,352		250,672 <sup>(5)</sup>
SERP					
Stephen J. Rotella	2,610,751		(366,308)		13,476,894 <sup>(6)</sup>
Deferred Compensation Plan		153,592	4,483		176,704 <sup>(5)</sup>
SERP					
James B. Corcoran					
Deferred Compensation Plan		3,440	80		3,520 <sup>(5)</sup>
SERP					
Ronald J. Cathcart					
Deferred Compensation Plan		35,632	833		36,465 <sup>(5)</sup>
SERP					
Fay L. Chapman	213,340		(193,461)		1,895,222
Deferred Compensation Plan		52,572	15,505		365,975 <sup>(5)</sup>
SERP			6,565 <sup>(4)</sup>		116,227
SERAP					

(1) The amounts reported in this column represent deferrals of compensation by the named executives into our Deferred Compensation Plan, a nonqualified unsecured plan described in the narrative below. We make no contributions into that plan on behalf of any of the named executives.

(2) The amounts reported in this column represent amounts credited to the account of each named executive during 2007 pursuant to our SERP described below and reported as 2007 compensation in the Summary Compensation Table on page 103.

(3) The significant decline in Mr. Killinger's Deferred Compensation Plan balance in 2007 resulted from his selection of the Phantom Stock method of earnings credits (described below) and the significant decline in our stock price during 2007.

(4) Mr. Killinger and Ms. Chapman were eligible for a benefit under the SERAP because both satisfied the previous age and service requirements under the plan.

(5) As of December 31, 2007, each named executive is vested in his or her SERP benefit reported above as follows: Mr. Killinger: 100%, Mr. Casey: 100%, Mr. Rotella: 50%, Mr. Corcoran: 0%, Mr. Cathcart: 25%, Ms. Chapman: 100%. Of the amounts shown, the following amounts were reported in the Summary Compensation Table in our definitive proxy



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statement filed March 19, 2007 (the "2007 Summary Compensation Table"), which was our first proxy statement filed under the SEC's new executive compensation disclosure rules: Mr. Killinger: \$346,800, Mr. Casey: \$68,142, Mr. Rotella: \$18,200.

(6)

\$1,885,680 of this amount was reported as part of Mr. Rotella's 2006 compensation in the 2007 Summary Compensation Table.

### Deferred Compensation Plan

We maintain a nonqualified unsecured Deferred Compensation Plan that allows certain highly compensated employees, including the named executives, to defer compensation. The amounts deferred into this plan and all earnings remain subject to claims of our general creditors until distributed upon a date or event selected by the participant. Eligible employees may elect to defer regular pay, bonuses, gains on exercise of nonqualified stock options, compensation related to the lapse of restrictions on restricted stock, and issuance of common stock or cash in satisfaction of performance share awards. Plan account balances are credited with earnings based on a participant's selection of one or more of the following methods:

*Interest Method.* This method credits interest at a rate equal to the rate at which unsecured junior debt would be issued. If we did not issue any unsecured junior debt for the year, then the comparable rate for peer institutions is used. We establish this rate on September 30 of the previous year (2007 interest rate: 5.83%).

*Phantom Stock.* This method tracks the performance of our common stock (2007 rate of return: (68.25%)).

*Vanguard Institutional Index Fund.* This fund tracks the performance of the Standard & Poor's 500 Index (2007 rate of return: 5.5%).

*Vanguard Small-Cap Index Fund.* This fund tracks the Morgan Stanley Capital International ("MSCI") U.S. Small Cap 1750 Index (2007 rate of return: 1.29%).

*Vanguard Developed Markets Index Fund.* This fund tracks the MSCI Europe and Pacific Region Index (2007 rate of return: 10.99%).

The rates of return for these earnings methods (other than the Interest Method) may be positive or negative and thus may result in gains or losses to a participant's plan balance. At the time of deferral of any item of compensation, each participant elects the payment commencement date, the earnings accrual method, and the form of payment. The earnings accrual method may be changed by the participant no more than one time per month. Available forms of payment are either lump sum or, if the participant's balance exceeds \$100,000, installment payments for a period of up to ten years. We do not make any contributions into the plan on behalf of participants or match any amounts deferred pursuant to the plan, other than dividend equivalents for balances with earnings accrual credits based on the Phantom Stock method. In compliance with Section 409A of the Code, the payment election must be made at least one year before the distribution. In accordance with applicable SEC rules, we reported compensation deferred into the plan as compensation to the named executive for the year earned.

In 2007, under the transition rules of Internal Revenue Code Section 409A, we allowed participants to make a one-time election to accelerate distributions of previously deferred compensation. This one-time election provided for payments of a lump sum or up to ten annual installments for those whose balance exceeded \$100,000. Lump sum or installment payments will begin in July 2008. Of the named executives, Messrs. Killinger and Casey and Ms. Chapman chose to accelerate payment of their full balances in the plan.

### **Supplemental Employees' Retirement Plan**

The SERP is a non-qualified plan designed to provide certain highly compensated employees, including the named executives, with benefits they would have otherwise received under the WaMu Pension Plan, but for certain restrictions set forth in the Code on the amount of compensation that may be considered as eligible compensation pursuant to the Pension Plan. The SERP is designed to provide participants with a benefit credit equal to the benefit credit they would have received under the Pension Plan (between 4% and 8%, depending on their years of service) had their eligible compensation under the Pension Plan not been limited by applicable restrictions contained in the Code. In addition, an individual's SERP benefit vests over a five-year period and is credited with earnings at an annual rate that is established in the same manner as the Pension Plan rate discussed above. We establish the rate on November 30 of the prior year, and during 2007 the applicable interest rate for this plan was 4.52%. In compliance with Section 409A of the Code, six months after termination of service for a participant who is a "specified" or "key" employee under Section 409A, the participant will receive a lump sum payment equal to his or her total benefit, except that any participant with a total benefit in excess of \$100,000 may elect to receive annual installment payments over a period of up to ten years, if in accordance with Section 409A of the Code, the election is made at least one year before the distribution.

### **Supplemental Executive Retirement Accumulation Plan**

The SERAP is a non-qualified plan designed to provide additional retirement benefits to the named executives and other executive officers. Prior to our adoption of the ETRIP in 2004, our executive officers, including the named executives, were eligible to receive benefit accruals under the SERAP based on a combination of age and service credits. None of the named executives receives any benefit accruals pursuant to the SERAP; however Mr. Killinger's SERAP benefit continues to receive interest credits. Pursuant to the SERAP, participants receive benefit credits of 1% for each year of Company executive service, with a minimum of 3% and a maximum of 12%. Participants also receive an interest credit based on the rate that would have been paid on our unsecured junior debt (if any) with a ten-year maturity. If we did not issue any unsecured junior debt for the year, then the comparable rate for peer institutions is used. We establish this rate during September of the previous year and for 2007, the applicable interest rate for this plan was 5.83%. The same distribution restrictions under Section 409A described for the SERP above also apply to the SERAP.

### **Deferred Bonus Arrangement**

Pursuant to his 1982 employment agreement with a company we acquired, Mr. Killinger is entitled to a deferred bonus arrangement that we assumed, pursuant to which certain of Mr. Killinger's deferred bonus amounts and accrued earnings payable to him by the predecessor company are payable by us to Mr. Killinger upon termination of his employment for any reason. Company credits are no longer made to this account and the balance is treated as having been invested in the *Principal Funds Equity Income I (A) Fund*. The rate of return on this account during 2007 was 4.72%, and as of December 31, 2007, the accrued benefits under this arrangement totaled \$352,170.

### **Potential Payments Upon Termination or Change-in-Control**

This section discusses the incremental compensation we would have to pay to each named executive in the event of a change-in-control of the Company or a termination of the named executive's employment with us for various described reasons, sometimes referred to in this section as a "triggering event." In accordance with applicable SEC rules, the following discussion assumes:

that the triggering event in question the death, disability, change-in-control or termination occurred on December 31, 2007, the last business day of 2007; and

with respect to calculations based on our stock price, we used \$13.61, which was the reported closing price of one share of our common stock on the NYSE on December 31, 2007.

In connection with any actual termination of employment, we may determine to enter into an agreement or to establish an arrangement providing additional benefits or amounts, or altering the terms of benefits described below, as deemed appropriate by the Human Resources Committee. The actual amounts that would be paid upon a named executive's termination of employment can be determined only at the time of such executive's separation from the Company. Due to the number of factors that affect the nature and amount of any benefits provided upon the events discussed below, any actual amounts paid or distributed may be higher or lower than reported below. Factors that could affect these amounts include the timing during the year of any such event, our stock price and the executive's age and service.

Various agreements and plans define each named executive's rights and obligations in the event of a triggering event. Specifically, each named executive other than Ms. Chapman is a party to an agreement with us called either an "employment agreement" or a "change-in-control agreement", and each named executive is a party to equity award agreements, and each is or may be a participant in various Company plans, including, without limitation, the Amended and Restated 2003 Equity Incentive Plan, the ETRIP, the SERP, the SERAP, the Leadership Bonus Plan and the new executive severance plan discussed at page 100. Ms. Chapman is a party to a severance agreement, discussed at page 101. These agreements and plans may provide that a named executive is entitled to additional consideration in the event of a triggering event. The change-in-control agreements of Messrs. Casey, Corcoran and Cathcart do not provide any material benefits or compensation to either named executive prior to a change-in-control of the Company; however, our new executive severance plan adopted in 2008 does.

The following is a general discussion of the primary categories of triggering events under the named executives' employment or change-in-control agreements and Company plans. Where the terms and consequences are unique with respect to a particular named executive, the differences are discussed in the footnotes to the table below for that named executive.

In the footnotes to the tables that follow this discussion, we also disclose the aggregate amount of vested other compensation each named executive could have realized if his or her employment terminated on December 31, 2007, regardless whether a triggering event occurred.

#### **Death or Disability**

The employment or change-in-control agreements we have with all named executives other than Ms. Chapman generally provide that we shall make no further cash payments to the named executive, or his estate, in the event of death or disability. Under Ms. Chapman's severance agreement, upon this triggering event Ms. Chapman would be entitled to receive all cash payments due to her under her severance agreement and related consulting agreement.

Upon death or disability, all of a named executive's unvested equity shall immediately vest as follows:

All unvested stock options vest and remain exercisable until the first to occur of (i) 12 months after the date of death or permanent disability or (ii) the original expiration date of the option.

All shares of restricted stock become vested to the extent of our achievement of the applicable Company performance measures for such shares (if any) as of the end of the relevant period.

With respect to performance share awards, the named executive or his or her estate receives a prorated award based on the number of weeks of employment during the performance period and prior to the triggering event. This is paid out at the end of the applicable performance cycle to the extent of our achieved performance relative to the peer group.



Upon death or disability, cash bonuses payable to a named executive under our Leadership Bonus Plan are prorated based on the number of days of active service during the calendar year prior to the triggering event. Our performance continues to be measured against the applicable performance measures at the end of the applicable calendar year.

Each named executive, or his or her beneficiaries, will receive payments or benefits under our Deferred Compensation Plan, SERP, SERAP and ETRIP, to the extent of their balances or accrued benefits, pursuant to the terms of those plans. These plans and the named executives' plan balances or accrued amounts, as applicable, are described in detail beginning at page 114. In general, each of these plans provides for the payment of a lump sum to the named executive or his or her estate if his or her balance is under a threshold amount, or installment payments under certain circumstances. Between the date of the applicable triggering event and the date benefits are distributed, each named executive's benefits under these plans continue to accrue earnings, and, with respect to the Deferred Compensation Plan, are adjusted by gains or losses based upon his or her investment elections. The benefits under these plans, other than the Deferred Compensation Plan, vest over an established schedule. The SERP and SERAP provide for an acceleration of the unvested balance upon the death or permanent disability of the executive, while the ETRIP provides no acceleration under those circumstances. In the employment or change-in-control agreement for each named executive other than Ms. Chapman, "termination due to disability" is generally defined as the named executive being unable to perform the essential functions of his job for a continuous period of 180 days.

#### **Termination of Employment by the Company without "Cause" before a Change-in-Control of the Company**

Messrs. Killinger and Rotella have employment agreements that provide for compensation payments and equity acceleration if we terminate their employment without "cause," as defined below, before there is a change-in-control of the Company. As discussed at page 100, in January 2008 the Human Resources Committee approved the material terms of a new executive severance plan in which Messrs. Casey, Corcoran and Cathcart will participate. Ms. Chapman will not participate in the new plan because she is no longer an executive officer. For purposes of this discussion and the tables that follow, we have assumed the new executive severance plan was effective as of December 31, 2007.

#### ***Equity Acceleration Messrs. Killinger and Rotella***

If we terminate Mr. Killinger or Mr. Rotella without cause and before a change-in-control of the Company, he would be entitled to equity acceleration as follows:

All unvested stock options and unvested shares of restricted stock would vest.

Mr. Rotella's performance share awards would continue for the remainder of the performance cycles pursuant to his employment agreement. Because he is over age 55 and has over 10 years of service, Mr. Killinger would not forfeit his performance share awards. In both cases, the payout of performance share awards, if any, would be made at the end of the applicable performance cycle to the extent of our achieved performance relative to its peer group.

#### ***Cash Payments Messrs. Killinger and Rotella***

Both Mr. Killinger and Mr. Rotella would be entitled to a lump sum cash severance payment six months after the date of termination. Mr. Killinger's severance amount would be equal to three times his "annual compensation" and Mr. Rotella's severance would equal two times his "annual compensation." For this purpose, "annual compensation" includes only the following:

Salary and bonus, calculated as: (i) the greatest of the executive's annual base salary for (A) the calendar year in which termination occurs, (B) the prior calendar year, or (C) (if applicable) the

calendar year immediately preceding the year in which the change-in-control occurred, plus (ii) the greatest of (A) the executive's unadjusted target bonus for the calendar year in which the termination occurs, (B) the executive's actual bonus (including, for the avoidance of doubt, any portion of the actual bonus that was deferred or exchanged at the executive's election for equity awards) for the prior calendar year, or (C) if applicable, the executive's actual bonus (including, for the avoidance of doubt, any portion of the actual bonus that was deferred or exchanged at the executive's election for equity awards) for the calendar year immediately preceding the year in which the change-in-control occurred;

Benefit accruals made (or anticipated to have been made during the remainder of the year) on behalf of the named executive under the WaMu Pension Plan and the SERP, and Company contributions on behalf of the named executive under the WaMu Savings Plan during the calendar year in which the termination occurs; and

The annualized contributions made on behalf of the named executive under our medical, dental, life and long-term disability plans during the calendar year in which the termination occurs.

At the Committee's discretion, cash bonus payments pursuant to our Leadership Bonus Plan would be prorated based on the number of days of active service during the calendar year prior to the termination. Company performance continues to be measured against the applicable performance measures at the end of the applicable calendar year.

#### *Cash Payments Other Named Executives*

Under our new executive severance plan, all executive officers other than Messrs. Killinger and Rotella, including Messrs. Casey, Corcoran and Cathcart, are entitled to a cash payment upon this triggering event equal to 1.5 times the sum of (i) base salary plus (ii) the higher of (A) target bonus for the current year or (B) actual bonus for the prior year. No benefits under the severance plan will be paid to any covered executive who becomes entitled to benefits under his or her change-in-control agreement.

Under Ms. Chapman's severance agreement, upon this triggering event Ms. Chapman would be entitled to receive all payments due to her under her severance agreement and related consulting agreement.

#### **Termination by Company with "Cause" or by the Named Executive for Any Reason before a Change-in-Control of the Company**

Our employment or change-in-control agreements with all named executives other than Ms. Chapman, and the new executive severance plan, provide that if we terminate the named executive with "cause" before there is a change-in-control of the Company, then the named executive would not be entitled to any cash severance payments. If Ms. Chapman materially breaches the terms of her severance agreement or related consulting agreement at any time whether before or after a change-in-control of the Company, then she would not be entitled to any further payments under either agreement. In addition, in case of a "for cause" termination, all of each named executive's outstanding stock options (whether vested or unvested), unvested shares of restricted stock and performance share awards for outstanding performance cycles would be immediately forfeited and cancelled pursuant to the applicable equity award agreements. The named executive's cash bonus payout under our Leadership Bonus Plan for the year in which the termination occurred would be forfeited at the discretion of the Human Resources Committee. The employment and change-in-control agreements generally define "cause" to include (i) recurring violations of our substance abuse policy; (ii) conviction of a felony or certain misdemeanors involving moral turpitude; (iii) entering into a pretrial diversion program in connection with the prosecution for certain crimes; (iv) dishonesty, fraud, destruction or

theft of Company property; (v) physical attack on another Company employee; (vi) willful malfeasance or gross negligence in performance; or (vii) or misconduct that causes a material injury to us.

The plan documents for our nonqualified retirement plans, the SERP, SERAP and ETRIP, all generally provide that if the "for cause" termination of the named executive is due to his or her fraud, embezzlement, theft or any other crime of moral turpitude or dishonesty in his or her relationship with us (without necessity of formal criminal proceedings being initiated), then the named executive's vested and unvested benefits in these plans also would be forfeited.

If the named executive terminates his or her employment for any reason prior to a change-in-control, the employment and change-in-control agreements and plan documents (and severance and consulting agreements for Ms. Chapman) do not provide for any additional compensation or benefits for such named executive. However, the named executive would not forfeit his or her equity awards and retirement plan balances, as described above.

#### **Upon a Change-in-Control of the Company without Termination of the Named Executive's Employment**

The named executives' employment and change-in-control agreements and Ms. Chapman's severance and consulting agreements do not provide for any additional compensation payable to the named executives in the event of a change-in-control of the Company (*e.g.*, no "single trigger" payment). However, our Amended and Restated 2003 Equity Incentive Plan provides that as of the consummation of a "company transaction," all outstanding unvested stock options and unvested shares of restricted stock would vest, unless the Human Resources Committee instead in its discretion provides that such outstanding awards are assumed or substituted by the acquiring company with all existing terms and conditions, including vesting terms, remaining in effect. For this purpose, "company transaction" is generally defined in the Plan as an acquisition of the Company by merger, consolidation, asset acquisition or stock purchase, which is generally the same as a change-in-control of the Company.

As of the closing of the change-in-control (whether or not the named executive is later terminated), the named executives would receive a payout for all performance share awards subject to outstanding performance cycles. The payout would be based on our performance relative to the peer group, as calculated through the most recent month or quarter prior to the date of the change-in-control. In addition, our ETRIP provides that each named executive would be credited with three additional years of "executive service" for the purposes of ETRIP benefit calculations. The SERP and SERAP do not have any acceleration or similar provisions regarding a change-in-control.

#### **Within Three Years after a Change-in-Control of the Company: Termination by the Company for Any Reason or without Cause, as Applicable, or by the Named Executive with Good Reason**

In accordance with their employment or change-in-control agreements and applicable benefit plan documents, each named executive other than Ms. Chapman would receive the amounts described in the section entitled "Death or Disability" with any performance criteria related to restricted stock vesting removed, as well as a lump sum cash severance payment equal to three times the named executive's "annual compensation" in the event that they are terminated for any reason (for Messrs. Killinger and Rotella) or without cause (for Messrs. Casey, Corcoran and Cathcart) or if they terminate their employment with "good reason," in all cases within three years after a change-in-control of the Company. For this purpose, annual compensation would be calculated in accordance with the description above at page 122.

For Messrs. Killinger and Rotella, "good cause" or "good reason" is generally defined as any of the following: (i) assignment of duties that are materially different from those assigned prior to the change-in-control, or which result in significantly less authority and responsibility; (ii) the removal of named executive from the position held immediately prior to the change-in-control; (iii) a reduction in

base salary, or failure to increase base salary each year in a percentage amount at least equal to that of the consumer price index; (iv) a reduction in the named executive's total compensation to a level below the average total compensation paid by the Company to the named executive during the 24 months prior to the change-in-control; or (v) any change in job duties requiring relocation outside of the greater metropolitan area of the primary work location without the employee's written consent. In addition, Mr. Rotella's agreement further defines "good reason" to include (a) the failure of a successor to the Company to assume all of our obligations under the agreement and any related arrangement; or (b) a material breach of the agreement by the Company or its successor.

For other named executives other than Ms. Chapman, "good reason" is generally defined as any of the following: (i) the assignment of duties which (a) are materially different from the executive's duties immediately prior to the change-in-control, or (b) result in the executive having significantly less authority and/or responsibility than he or she had prior to the change-in-control; (ii) a reduction of executive's total compensation opportunity from that in effect on the date of the change-in-control, with the exception that changes in the allocation of the executive's compensation between salary and incentive compensation, and changes to the criteria or method for determining incentive compensation amounts actually earned, shall not constitute "good reason"; or (iii) a relocation by more than 50 miles of the executive's principal place of employment as in effect on the date of the change-in-control, if the relocation increases the distance between the executive's principal residence and principal place of employment by more than 25 miles.

The amount we would owe Ms. Chapman if we terminated her for any reason other than her material breach of the terms of her severance or consulting agreement does not change whether or not a change-in-control occurs.

#### **Within Three Years after a Change-in-Control of the Company: Termination by the Named Executive without Good Reason**

If the named executive terminates his or her employment without "good reason" within three years after a change-in-control, the employment and change-in-control agreements and plan documents and, for Ms. Chapman, her severance and consulting agreements, do not provide for any additional compensation or benefits.

#### **280G Tax Gross-Up**

Our employment and change-in-control agreements with named executives other than Ms. Chapman provide that if any Company payment made upon termination after a change-in-control of the Company constitutes an "excess parachute payment" under Section 280G of the Code, we would make a gross-up payment to the named executive. The gross-up payment would be equal to the amount necessary to cause the net amount retained by the named executive, after subtracting (i) the excise tax imposed on "excess parachute payments" by Section 4999 of the Code, and (ii) any federal, state and local income taxes, FICA tax, and the Section 4999 excise tax on the gross-up payment, to be equal to the net amount the named executive would have retained had no Section 4999 excise tax been imposed and no Company gross-up payment been made. Ms. Chapman's severance agreement does not provide for any gross-up payment.

#### **Post-Employment Recoupment of Equity Awards**

The award agreements for restricted stock and stock option grants made in 2006 and beyond to employees, including the named executives, contain certain non-solicitation restrictions that generally apply for one-year after termination of the named executive's employment with us. If the named executive violates the non-solicitation provisions, he or she will forfeit all of his or her outstanding stock options and restricted stock awarded under the agreement. In addition, the named executive

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would be required to return to us all gains realized by him or her on restricted stock or stock options obtained pursuant to the agreements during the 12 month period prior to his or her violation.

**Kerry K. Killinger**

Type of Benefit	Termination After Change-in-Control <sup>(7)(8)</sup>				
	A	B	C	D	E
	Death or Disability (\$)	Termination before a Change- in-Control by Company without Cause (\$)	Upon a Change-in- Control (\$) <sup>(7)</sup>	Termination by Company for Any Reason or by Executive with Good Reason (\$)	Termination by Executive without Good Reason (\$)
Cash Severance <sup>(1)</sup>		16,491,635		16,491,635	
Option Vesting <sup>(2)</sup>					
Restricted Stock Vesting <sup>(3)</sup>	1,526,736	5,835,945	5,835,945		
Performance Share Vesting <sup>(4)</sup>					
ETRIIP Additional Service Credits			3,956,073		
280G Tax Gross Up <sup>(5)</sup>					
Total Value Upon Event <sup>(6)</sup>	1,526,736	22,327,580	9,792,018	16,491,635	
Total Value Upon CIC and Termination Events in Column D (Column C+D)				26,283,653	
Total Value Upon CIC and Termination Event in Column E (Column C+E)					9,792,018

(1) Mr. Killinger's employment agreement provides for a lump sum cash payment in the amount of three times his "annual compensation," as described at page 122, in the event (i) we terminate his employment, without cause, prior to a change-in-control; or (ii) if within three years following a change-in-control, our successor terminates his employment for any reason or by Mr. Killinger for good reason.

(2) Mr. Killinger's employment agreement provides for the acceleration of vesting of stock options and restricted stock upon his termination (i) by us for any reason other than for cause preceding a change-in-control, or (ii) after a change-in-control, by our successor for any reason or by Mr. Killinger for good reason (assuming the vesting of his options and stock does not accelerate on the closing of the change-in-control). The value of stock option vesting reflected in the table is zero as none of his unvested options has an exercise price less than the \$13.61 closing price of our stock on December 31, 2007. Because Mr. Killinger meets the age and service requirements for retirement under his stock option agreements (age 55 with 10 years of service), his post-termination exercise period for vested options is 5 years, not to exceed the original expiration date of the option grant.

(3) The value of restricted stock vesting was calculated by multiplying the number of unvested shares by \$13.61, with any performance measures through the end of 2007 factored into the calculation for Death or Disability but not for a Change-in-Control.

(4) This reflects the anticipated payout rate for performance share awards with uncompleted performance cycles as of December 31, 2007.

(5) Mr. Killinger's employment agreement provides that if any Company payments made upon termination after a change-in-control of the Company constitute a "parachute payment" under Section 280G of the Code, the Company would make a gross-up payment to Mr. Killinger. The gross-up payment would be equal to the amount necessary to cause the net amount retained by Mr. Killinger, after subtracting (i) the parachute payment excise tax imposed by Section 4999 of the Code, and (ii) any federal, state and local income taxes, FICA tax, and the Section 4999 excise tax on the gross-up payment, to be equal to the net amount Mr. Killinger would have retained had no Section 4999 excise tax been imposed and no Company gross-up payment been made.

(6)

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In addition to the total values payable to Mr. Killinger upon each of the triggering events contained in this table, Mr. Killinger would have been entitled to receive or retain the following amounts, none of which would have increased or

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accelerated on his termination or a change-in-control of the Company: (i) all of his vested stock options reported at page 108, unless he is terminated for cause; (ii) his accrued benefits under our nonqualified deferred compensation plans, as reported at page 118, unless in the case of the SERP and SERAP he is terminated for cause; (iii) his accrued benefits under the WaMu Pension Plan, as reported at page 114, and unless he is terminated for cause, his accrued benefits under the ETRIP, as reported in footnote 3 to the Pension Benefits Table at page 114; (iv) his accrued benefits or amounts under Company plans that do not discriminate in favor of executive officers and that are available generally to all salaried employees, such as the WaMu Savings (401(k)) Plan; and (v) the deferred bonus arrangement described on page 120. As of December 31, 2007, the aggregate of these amounts was \$19,972,267, or \$8,986,004 if Mr. Killinger had been terminated for cause.

(7)

These columns assume that the vesting of stock options and restricted stock accelerated on the consummation of the change-in-control because the Human Resources Committee did not provide for the assumption or substitution of unvested stock options and restricted stock by the acquiring company.

(8)

Note: For a change-in-control and subsequent termination of Mr. Killinger's employment, he would have received the "Total Value Upon Event" specified in the table in column C plus the "Total Value Upon Event" in either column D or column E, depending upon the circumstances of his termination.

Thomas W. Casey

Type of Benefit	Termination After Change-in-Control <sup>(7)(8)</sup>				
	A	B	C	D	E
	Death or Disability(\$)	Termination before a Change-in-Control by Company without Cause(\$)	Upon a Change-in-Control(\$) <sup>(7)</sup>	Termination by Company without Cause or by Executive with Good Reason(\$)	Termination by Executive without Good Reason(\$)
Cash Severance <sup>(1)</sup>		3,042,090		6,287,391	
Option Vesting <sup>(2)</sup>					
Restricted Stock Vesting <sup>(3)</sup>	610,032		2,467,905		
Performance Share Vesting <sup>(4)</sup>					
ETRIP Additional Service Credits			1,438,865		
280G Tax Gross Up <sup>(5)</sup>				3,861,811	
Total Value Upon Event <sup>(6)</sup>	610,032	3,042,090	3,906,770	10,149,202	
Total Value Upon CIC and Termination Events in Column D (Column C+D)				14,055,972	
Total Value Upon CIC and Termination Event in Column E (Column C+E)					3,906,770

- (1) Mr. Casey's change-in-control agreement provides for a lump sum cash payment in the amount of three times his "annual compensation," as described at page 122, if within three years following a change-in-control, our successor terminates his employment without cause or if Mr. Casey terminates his employment for good reason. In addition, his agreement contains provision that prohibits him from soliciting our employees, contractors or consultants to join one of our competitors, which would apply for one-year after termination of his employment. The amount shown in Column B represents payments we would have made under our new executive severance plan assuming it had been effective at December 31, 2007.
- (2) The value of stock option vesting reflected in the table is zero as none of the unvested options has an exercise price less than the \$13.61 closing price of our stock on December 31, 2007.
- (3) The value of restricted stock vesting was calculated by multiplying the number of unvested shares by \$13.61, with any performance measures through the end of 2007 factored into the calculation for Death or Disability but not for a Change-in-Control.
- (4) This reflects the anticipated payout rate for performance share awards with uncompleted performance cycles as of December 31, 2007.
- (5) Mr. Casey's change-in-control agreement provides that if any Company payments made upon termination after a change-in-control of the Company constitute a "parachute payment" under Section 280G of the Code, our successor would make a gross-up payment to Mr. Casey. The gross-up payment would be equal to the amount necessary to cause the net amount retained by Mr. Casey, after subtracting (i) the parachute payment excise tax imposed by Section 4999 of the Code, and (ii) any federal, state and local income taxes, FICA tax, and the Section 4999 excise tax on the gross-up payment, to be equal to the net amount Mr. Casey would have retained had no Section 4999 excise tax been imposed and no Company gross-up payment been made.
- (6) In addition to the total values payable to Mr. Casey upon each of the triggering events contained in this table, Mr. Casey would have been entitled to receive or retain the following amounts, none of which would have increased or accelerated on his termination or a change-in-control of the Company: (i) all of his vested stock options reported at page 108, unless he is terminated for cause; (ii) his accrued benefits under our nonqualified deferred compensation plans, as reported at page 118, unless in the case of the SERP and SERAP he is terminated for cause, (iii) his accrued benefits under the WaMu Pension Plan, as reported at page 114, and unless he is terminated for cause his accrued benefits under the ETRIP, as reported in footnote 3 to the Pension Benefits Table at page 114; (iv) his 2007 Leadership Bonus Plan cash bonus payout; and (v) his accrued benefits or amounts under



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Company plans that do not discriminate in favor of executive officers and that are available generally to all salaried employees, such as the WaMu Savings (401(k)) Plan. As of December 31, 2007, the aggregate of these amounts was \$5,145,839, or \$3,210,630 if Mr. Casey had been terminated for cause.

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(7) These columns assume that the vesting of stock options and restricted stock accelerated on the consummation of the change-in-control because the Human Resources Committee did not provide for the assumption or substitution of unvested stock options and restricted stock by the acquiring company.

(8) *Note:* For a change-in-control and subsequent termination of Mr. Casey's employment, he would have received the "Total Value Upon Event" specified in the table in column C plus the "Total Value Upon Event" in either column D or column E, depending upon the circumstances of his termination.

**Stephen J. Rotella**

Type of Benefit	Termination After Change-in-Control <sup>(10)(11)</sup>				
	A	B	C	D	E
	Death or Disability(\$)	Termination Before a Change-in-Control by Company without Cause(\$) <sup>(8)</sup>	Upon a Change-in-Control(\$) <sup>(10)</sup>	Termination by Company for Any Reason or by Executive with Good Reason(\$)	Termination by Executive without Good Reason(\$)
Cash Severance <sup>(1)</sup>		8,451,952		12,677,928	
Option Vesting <sup>(2)</sup>					
Restricted Stock Vesting <sup>(3)</sup>	1,663,069	4,114,717 <sup>(9)</sup>	4,114,717		
Performance Share Vesting <sup>(4)</sup>					
ETRIP Additional Service Credits			3,953,848		
SERP Vesting <sup>(5)</sup>	88,352				
280G Tax Gross Up <sup>(6)</sup>				7,770,005	
Total Value Upon Event <sup>(7)</sup>	1,751,421	12,566,669	8,068,565	20,447,933	
Total Value Upon CIC and Term. Events in Column D (Column C+D)				28,516,498	
Total Value Upon CIC and Term. Event in Column E (Column C+E)					8,068,565

(1) Mr. Rotella's employment agreement provides for a lump sum cash payment in the amount of (i) two times his "annual compensation," as described at page 122, in the event the Company terminates his employment, without cause, prior to a change-in-control; and (ii) three times his annual compensation if within three years following a change-in-control, his employment is terminated by the Company for any reason or by Mr. Rotella for good reason.

(2) Mr. Rotella's employment agreement provides for the acceleration of vesting of stock options and restricted stock upon his termination (i) by the Company for any reason other than for cause preceding a change-in-control, or (ii) after a change-in-control, by the Company for any reason or by Mr. Rotella for good reason (assuming the options and stock does not accelerate on the closing of the change-in-control). In addition, upon such terminations, Mr. Rotella would continue to hold his performance share awards for all uncompleted performance cycles. Such awards would pay out at the end of the applicable cycles in accordance with the terms of the Performance Share Award Program. The value of stock option vesting reflected in the table is zero as none of the unvested options has an exercise price less than the \$13.61 closing price of our stock on December 31, 2007.

(3) The value of restricted stock vesting was calculated by multiplying the number of unvested shares by \$13.61, with any performance measures through the end of 2007 factored into the calculation for Death or Disability but not for a Change-in-Control.

(4)

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This reflects the anticipated payout rate for performance share awards with uncompleted performance cycles as of December 31, 2007.

- (5) Mr. Rotella was 50% vested in his SERP benefit as of the end of 2007. This amount represents the portion of Mr. Rotella's SERP benefit that would become non-forfeitable upon his death or permanent disability. There is no incremental value to Mr. Rotella in other termination situations.
- (6) Mr. Rotella's employment agreement provides that if any Company payments made upon termination after a change-in-control of the Company constitute a "parachute payment" under Section 280G of the Code, the Company would make a gross-up payment to Mr. Rotella. The gross-up payment would be equal to the amount necessary to cause the net

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amount retained by Mr. Rotella, after subtracting (i) the parachute payment excise tax imposed by Section 4999 of the Code, and (ii) any federal, state and local income taxes, FICA tax, and the Section 4999 excise tax on the gross-up payment, to be equal to the net amount Mr. Rotella would have retained had no Section 4999 excise tax been imposed and no Company gross-up payment been made.

- (7) In addition to the total values payable to Mr. Rotella upon each of the triggering events contained in this table, Mr. Rotella would have been entitled to receive or retain the following amounts, none of which would have increased or accelerated on his termination or a change-in-control of the Company: (i) all of his vested stock options reported at page 108, unless he is terminated for cause; (ii) his accrued benefits under our nonqualified deferred compensation plans, as reported at page 118, unless in the case of the SERP he is terminated for cause; (iii) his accrued benefits under the WaMu Pension Plan, as reported at page 114 and his accrued benefits under the ETRIP, as reported in footnote 3 to the Pension Benefits Table at page 114, in each case unless he is terminated for cause; (iv) his 2007 Leadership Bonus Plan cash bonus payout; and (v) his accrued benefits or amounts under Company plans that do not discriminate in favor of executive officers and that are available generally to all salaried employees, such as the WaMu Savings (401(k)) Plan. As of December 31, 2007, the aggregate of these amounts was \$15,465,672, or \$13,495,795 if Mr. Rotella had been terminated for cause.
- (8) Under Mr. Rotella's employment agreement, he would be required to execute a separation agreement with the Company upon termination to receive the benefits reported in this column. The separation agreement would contain a 24 month non-competition and non-solicitation covenant in favor of the Company.
- (9) Mr. Rotella's employment agreement provides that the Human Resources Committee may exclude any of his particular awards of restricted stock made after March 1, 2005 from acceleration upon the triggering event reported in this column.
- (10) These columns assume that the vesting of stock options and restricted stock accelerated on the consummation of the change-in-control because the Human Resources Committee did not provide for the assumption or substitution of unvested stock options and restricted stock by the acquiring company.
- (11) Note: For a change-in-control and subsequent termination of Mr. Rotella's employment, he would have received the "Total Value Upon Event" specified in the table in column D plus the "Total Value Upon Event" in either column E or column F, depending upon the circumstances of his termination.

### **James B. Corcoran**

Type of Benefit	A Death or Disability (\$)	B Termination Before a Change-in- Control by Company without Cause(\$)	C Upon a Change-in- Control(\$) <sup>(8)</sup>	Termination After Change-in-Control <sup>(8)(9)</sup>	
				D Termination by Company without Cause or by Executive with Good Reason(\$)	E Termination by Executive without Good Reason(\$)
Cash Severance <sup>(1)</sup>		2,329,800		4,692,672	
Option Vesting <sup>(2)</sup>					
Restricted Stock Vesting <sup>(3)</sup>	253,421		424,229		
Performance Share Vesting <sup>(4)</sup>					
ETRIP Additional Service Credits			1,068,458		
SERP Vesting <sup>(5)</sup>	3,520				
280G Tax Gross Up <sup>(6)</sup>					
Total Value Upon Event <sup>(7)</sup>	256,941	2,329,800	1,492,687	4,692,672	
Total Value Upon CIC and Term. Events in Column D (Column C+D)				6,185,359	
Total Value Upon CIC and Term. Event in Column E (Column C+E)					1,492,687

(1)

Mr. Corcoran's change-in-control agreement provides for a lump sum cash payment in the amount of three times his "annual compensation," as described at page 122, if within three years following a change-in-control, our successor terminates his employment without cause or Mr. Corcoran terminates his employment for good reason. In addition, his agreement contains provision that prohibits him from soliciting our employees, contractors or consultants to join one of our competitors, which would apply for one-year after termination of his employment. The amount shown in Column B

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represents payments we would have made under our new executive severance plan assuming it had been effective at December 31, 2007.

- (2) The value of stock option vesting reflected in the table is zero as none of the unvested options has an exercise price less than the \$13.61 closing price of our stock on December 31, 2007.
- (3) The value of restricted stock vesting was calculated by multiplying the number of unvested shares by \$13.61, with any performance measures through the end of 2007 factored into the calculation for Death or Disability but not for a Change-in-Control.
- (4) This reflects the anticipated payout rate for performance share awards with uncompleted performance cycles as of December 31, 2007.
- (5) Mr. Corcoran was 0% vested in his SERP benefit as of the end of 2007. This amount represents the portion of Mr. Corcoran's SERP benefit that would become non-forfeitable upon his death or permanent disability. There is no incremental value to Mr. Corcoran in other termination situations.
- (6) Mr. Corcoran's change-in-control agreement provides that if any Company payments made upon termination after a change-in-control of the Company constitute a "parachute payment" under Section 280G of the Code, the Company would make a gross-up payment to Mr. Corcoran. The gross-up payment would be equal to the amount necessary to cause the net amount retained by Mr. Corcoran, after subtracting (i) the parachute payment excise tax imposed by Section 4999 of the Code, and (ii) any federal, state and local income taxes, FICA tax, and the Section 4999 excise tax on the gross-up payment, to be equal to the net amount Mr. Corcoran would have retained had no Section 4999 excise tax been imposed and no Company gross-up payment been made.
- (7) In addition to the total values payable to Mr. Corcoran upon each of the triggering events contained in this table, Mr. Corcoran would have been entitled to receive or retain the following amounts, none of which would have increased or accelerated on his termination or a change-in-control of the Company: (i) all of his vested stock options reported at page 108, unless he is terminated for cause; (ii) his accrued benefits under our nonqualified deferred compensation plans, as reported at page 118, unless in the case of the SERP he is terminated for cause; (iii) his accrued benefits under the WaMu Pension Plan, as reported at page 114 and his accrued benefits under the ETRIP, as reported in footnote 3 to the Pension Benefits Table at page 114, in each case unless he is terminated for cause; (iv) his 2007 Leadership Bonus Plan cash bonus payout; and (v) his accrued benefits or amounts under Company plans that do not discriminate in favor of executive officers and that are available generally to all salaried employees, such as the WaMu Savings (401(k)) Plan. As of December 31, 2007, the aggregate of these amounts was \$389,742, or \$9,146 if Mr. Corcoran had been terminated for cause.
- (8) These columns assume that the vesting of stock options and restricted stock accelerated on the consummation of the change-in-control because the Human Resources Committee did not provide for the assumption of unvested stock options and restricted stock by the acquiring company.
- (9) Note: For a change-in-control and subsequent termination of Mr. Corcoran's employment, he would have received the "Total Value Upon Event" specified in the table in column C plus the "Total Value Upon Event" in either column D or column E, depending upon the circumstances of his termination.

Ronald J. Cathcart

Type of Benefit	Termination After Change-in-Control <sup>(8)(9)</sup>				
	A	B	C	D	E
	Death or Disability (\$)	Termination before a Change-in-Control by Company without Cause (\$)	Upon a Change-in-Control (\$) <sup>(8)</sup>	Termination by Company without Cause or by Executive with Good Reason (\$)	Termination by Executive without Good Reason (\$)
Cash Severance <sup>(1)</sup>		1,673,700		3,417,141	
Option Vesting <sup>(2)</sup>					
Restricted Stock Vesting <sup>(3)</sup>	161,360		834,489		
Performance Share Vesting <sup>(4)</sup>					
ETRIP Additional Service Credits			855,069		
SERP Vesting <sup>(5)</sup>	27,349				
280G Tax Gross Up <sup>(6)</sup>				1,869,620	
Total Value Upon Event <sup>(7)</sup>	188,709	1,673,700	1,689,558	5,286,761	
Total Value Upon CIC and Term. Events in Column D (Column C+D)				6,976,319	
Total Value Upon CIC and Term. Event in Column E (Column C+E)					1,689,558

(1) Mr. Cathcart's change in control agreement provides for a lump sum cash payment in the amount of three times his "annual compensation," as described at page 122, if within three years following a change-in-control, our successor terminates his employment without cause or Mr. Cathcart terminates his employment for good reason. In addition, his agreement contains provision that prohibits him from soliciting our employees, contractors or consultants to join one of our competitors, which would apply for one-year after termination of his employment. The amount shown in Column B represents payments we would have made under our new executive severance plan assuming it had been effective at December 31, 2007.

(2) The value of stock option vesting reflected in the table is zero as none of the unvested options has an exercise price that is less than the \$13.61 closing price of our stock on December 31, 2007.

(3) The value of restricted stock vesting was calculated by multiplying the number of unvested shares by \$13.61, with any performance measures through the end of 2007 factored into the calculation for Death or Disability but not for a Change-in-Control.

(4) This reflects the anticipated payout rate for performance share awards with uncompleted performance cycles as of December 31, 2007.

(5) Mr. Cathcart was 25% vested in his SERP benefit as of the end of 2007. This amount represents the portion of Mr. Cathcart's SERP benefit that would become non-forfeitable upon his death or permanent disability. There is no incremental value to Mr. Cathcart in other termination situations.

(6) Mr. Cathcart's change in control agreement provides that if any Company payments made upon termination after a change-in-control of the Company constitute a "parachute payment" under Section 280G of the Code, the Company would make a gross-up payment to Mr. Cathcart. The gross-up payment would be equal to the amount necessary to cause the net amount retained by Mr. Cathcart, after subtracting (i) the parachute payment excise tax imposed by Section 4999 of the Code, and (ii) any federal, state and local income taxes, FICA tax, and the Section 4999 excise tax on the gross-up payment, to be equal to the net amount Mr. Cathcart would have retained had no Section 4999 excise tax been imposed and no Company gross-up payment been made.

(7)

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In addition to the total values payable to Mr. Cathcart upon each of the triggering events contained in this table, Mr. Cathcart would have been entitled to receive or retain the following amounts, none of which would have increased or accelerated on his termination or a change-in-control of the Company: (i) all of his vested stock options reported at page 108, unless he is terminated for cause; (ii) his accrued benefits under our nonqualified deferred compensation plans,



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as reported at page 118, unless in the case of the SERP he is terminated for cause; (iii) his accrued benefits under the WaMu Pension Plan, as reported at page 114 and his accrued benefits under the ETRIP, as reported in footnote 3 to the Pension Benefits Table at page 114, in each case unless he is terminated for cause; (iv) his 2007 Leadership Bonus Plan cash bonus payout; and (v) his accrued benefits or amounts under Company plans that do not discriminate in favor of executive officers and that are available generally to all salaried employees, such as the WaMu Savings (401(k)) Plan. As of December 31, 2007, the aggregate of these amounts was \$340,895, or \$9,450 if Mr. Cathcart had been terminated for cause.

(8) These two columns assume that the vesting of stock options and restricted stock accelerated on the consummation of the change-in-control because the Human Resources Committee did not provide for the assumption of unvested stock options and restricted stock by the acquiring company.

(9) Note: For a change-in-control and subsequent termination of Mr. Cathcart's employment, he would have received the "Total Value Upon Event" specified in the table in column C plus the "Total Value Upon Event" in either column D or column E, depending upon the circumstances of his termination.

### Fay L. Chapman

Type of Benefit	Termination After Change-in-Control <sup>(6)(7)</sup>				
	A	B	C	D	E
	Death or Disability (\$)	Termination before a Change- in-Control by Company without Cause (\$)	Upon a Change-in- Control (\$) <sup>(6)</sup>	Termination by Company without Cause or by Executive with Good Reason (\$)	Termination by Executive without Good Reason (\$)
Cash Severance <sup>(1)</sup>	3,181,000	3,181,000		3,181,000	
Option Vesting <sup>(2)</sup>					
Restricted Stock Vesting <sup>(3)</sup>	457,886		1,375,785		
Performance Share Vesting <sup>(4)</sup>					
ETRIP Additional Service Credits			1,065,505		
280G Tax Gross Up					
Total Value Upon Event <sup>(5)</sup>	3,638,886	3,181,000	2,441,290	3,181,000	
Total Value Upon CIC and Term. Events in Column D (Column C+D)				5,622,290	
Total Value Upon CIC and Term. Event in Column E (Column C+E)					2,441,290

(1) Amounts shown represent \$531,000 in base salary through June 30, 2008 under the terms of Ms. Chapman's severance agreement and \$2,650,000 in consulting fees payable under her consulting agreement to be effective July 1, 2008. For purposes of cash severance, "cause" for Ms. Chapman means a material breach by her of the terms of her severance agreement, and "good reason" means a material breach by us of the terms of her severance agreement.

(2) The value of stock option vesting reflected in the table is zero as none of the unvested options has an exercise price that is less than the \$13.61 closing price of our stock on December 31, 2007.

(3) The value of restricted stock vesting was calculated by multiplying the number of unvested shares by \$13.61, with any performance measures through the end of 2007 factored into the calculation for Death or Disability but not for a Change-in-Control.

(4) This reflects the anticipated payout rate for performance share awards with uncompleted performance cycles as of December 31, 2007.

(5)

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In addition to the total values payable to Ms. Chapman upon each of the triggering events contained in this table, Ms. Chapman would have been entitled to receive or retain the following amounts, none of which would have increased or accelerated on her termination or a change-in-control of the Company: (i) all of her vested stock options reported at page 108, unless she is terminated for cause; (ii) her accrued benefits under our nonqualified deferred compensation plans, as reported at page 118, unless in the case of the SERP and SERAP she is terminated for cause; (iii) her accrued benefits

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under the WaMu Pension Plan, as reported at page 114, and unless she is terminated for cause, her accrued benefits under the ETRIP, as reported in footnote 3 to the Pension Benefits Table at page 114; (iv) her 2007 Leadership Bonus Plan cash bonus payout; and (v) her accrued benefits or amounts under Company plans that do not discriminate in favor of executive officers and that are available generally to all salaried employees, such as the WaMu Savings (401(k)) Plan. As of December 31, 2007, the aggregate of these amounts was \$4,293,215, or \$2,077,318 if Ms. Chapman had been terminated for cause.

- (6) These columns assume that the vesting of stock options and restricted stock accelerated on the consummation of the change-in-control because the Human Resources Committee did not provide for the assumption of unvested stock options and restricted stock by the acquiring company.
- (7) *Note:* For a change-in-control and subsequent termination of Ms. Chapman's employment, she would have received the "Total Value Upon Event" specified in the table in column C plus the "Total Value Upon Event" in either column D or column E, depending upon the circumstances of her termination.

### Compensation of Non-Employee Directors

Our Board of Directors, acting upon a recommendation from the Governance Committee, annually determines the non-employee directors' compensation for serving on the Board and its committees. In establishing non-employee director compensation, the Board and the Governance Committee are guided by the following goals:

Compensation should consist of a combination of cash and equity awards that are designed to pay the directors fairly for work required for a company of our size and scope;

Compensation should align the directors' interests with the long-term interests of shareholders; and

Compensation should assist with attracting and retaining qualified directors.

In making its recommendation, the Governance Committee considers information received from Towers Perrin, the compensation consulting firm, regarding competitive information on outside director compensation for *Fortune 500* companies generally and for the peer banks we use to benchmark executive compensation, as discussed at page 86. Towers Perrin also provides recommendations for our non-employee director compensation program. The chair of the Governance Committee engages Towers Perrin to perform the analysis provided to the Committee. The Governance Committee and Board most recently completed this process in December 2007, and determined that our director compensation for 2008 should change slightly from 2007, as noted below. We do not pay director compensation to directors who are also our employees. The elements of compensation paid to non-employee directors for their service on our Board are described below.

### Cash Compensation

Non-employee directors receive the following cash payments for their service on our Board of Directors and Board committees:

an annual cash retainer of \$60,000;

\$750 for attendance at each purely telephonic Board meeting or committee meeting;

\$1,500 for attendance in person or by telephone at each other Board meeting or committee meeting;

an annual retainer of \$10,000 to the chair of each of the Finance, Human Resources and Governance Committees;

an annual retainer of \$7,500 to the chair of the Corporate Relations Committee;

an annual retainer of \$20,000 to the chair of the Audit Committee (increased from \$15,000 in 2007); and

an annual retainer of \$25,000 for the Lead Independent Director (increased from \$5,000 in 2007).

Each Corporate Development Committee member other than Mr. Killinger receives an annual cash retainer of \$6,000 in lieu of any fees for committee meeting attendance.

Directors who resign or retire from our Board receive a prorated portion of the applicable cash retainers based upon their service on the Board and Board committees during the year. During 2007, we did not provide perquisites to any director in an amount that is reportable under applicable SEC rules and regulations. We directly pay or reimburse all non-employee directors for parking, travel and accommodation expenses in connection with attendance at Board and committee meetings. When a

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director retires from our Board, it is our practice to make a \$10,000 cash donation in the retiring director's name to a charitable entity selected by the director.

### Stock Compensation

Each non-employee director is eligible for an annual grant of options to purchase Company common stock and shares of restricted stock issued from our Amended and Restated 2003 Equity Incentive Plan, as recommended by our Governance Committee. The options and restricted stock we award to our directors vest on the first anniversary of the date of grant, subject to earlier vesting on termination of service in certain circumstances. Shares of restricted stock for directors accrue regularly-declared Company dividends in the form of additional shares of restricted stock.

### Deferred Compensation

Our directors are also eligible to participate in our Deferred Compensation Plan, which is described in greater detail at page 119. The Deferred Compensation Plan allows eligible directors to defer their vested restricted stock and their fees and retainers payable for their service on the Board and Board committees.

### Director Compensation in 2007

The table below shows compensation we paid our non-employee directors for 2007. Mr. Chazen is not included because he joined our Board in 2008.

Name	Fees Earned or Paid in Cash \$( <sup>1</sup> )	Stock Awards \$( <sup>2</sup> )	Option Awards \$( <sup>3</sup> )	Change in Pension Value and Nonqualified Deferred Compensation Earnings \$( <sup>4</sup> )	All Other Compensation \$( <sup>5</sup> )	Total (\$)
Anne V. Farrell	97,500	73,879	31,281			202,680
Stephen E. Frank	127,250	70,233	29,736	206	46,600	274,025
Thomas C. Leppert	82,750	25,190	29,736			137,676
Charles M. Lillis	90,000	25,190	29,736			144,926
Phillip D. Matthews	101,250	25,190	29,736			156,176
Regina T. Montoya	77,500	21,353	28,150			127,003
Michael K. Murphy	97,500	70,233	29,736			197,469
Margaret Osmer McQuade	94,500	70,233	29,736			194,469
Mary E. Pugh	96,250	70,233	29,736			196,219
William G. Reed Jr.	109,750	70,233	29,736			209,719
Orin C. Smith	90,750	70,233	29,736			190,719
James H. Stever	109,750	70,233	29,736			209,719

(1) The amounts in this column represent the annual cash retainers and cash meeting fees paid to our non-employee directors for service during 2007.

(2) This column reflects the dollar amount recognized for financial statement reporting purposes for 2007 in accordance with FAS 123R for awards of unvested restricted stock. The fair value of Company restricted stock is based on the market value of our common stock on the applicable measurement date for accounting purposes. For additional information, see Note 21 to the Washington Mutual, Inc. and Subsidiaries Consolidated Financial Statements contained in the Company's Form 10-K for the year-ended December 31, 2007. As of December 31, 2007, each non-employee director held the following number of shares of unvested restricted stock (including dividend shares) issued as stock awards: Mrs. Farrell: 3,452, Mr. Frank: 3,451, Mr. Leppert: 1,678,

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Mr. Lillis: 1,678, Mr. Matthews: 3,053, Ms. Montoya: 1,678, Mr. Murphy: 3,452, Ms. Osmer McQuade: 1,678, Ms. Pugh: 2,781, Mr. Reed: 3,452, Mr. Smith: 1,678, and Mr. Stever: 3,452. The grant date fair value computed in accordance with FAS 123R for each restricted stock award granted in 2007 and reported in this column was \$70,043.

(3)

This column reflects the dollar amount recognized for financial statement reporting purposes for 2007 in accordance with FAS 123R for stock option awards. For information regarding significant factors, assumptions and methodologies used in determining the fair value of our stock options, see Note 21 to the Washington Mutual, Inc. and Subsidiaries Consolidated Financial Statements contained in the Company's Form 10-K for the year-ended December 31, 2007, as supplemented by the table at page 107. The grant date fair value computed in accordance with FAS 123R for each stock option award granted in 2007 and reported in this column was \$29,696. As of December 31, 2007, each non-employee director held the following number of shares of vested and unvested Company stock options granted as option awards:

Name	Vested Stock Options	Unvested Stock Options
Anne V. Farrell	46,333	3,712
Stephen E. Frank	46,333	3,712
Thomas C. Leppert	3,333	3,712
Charles M. Lillis	3,333	3,712
Phillip D. Matthews	48,708	3,712
Regina T. Montoya	0	3,712
Michael K. Murphy	41,833	3,712
Margaret Osmer McQuade	21,018	3,712
Mary E. Pugh	37,333	3,712
William G. Reed Jr.	8,333	3,712
Orin C. Smith	3,333	3,712
James H. Stever	41,833	3,712

(4)

The amount shown for Mr. Frank represents above-market interest on his vested balance in an unfunded deferred compensation plan for certain former directors of Great Western Financial Corporation, for which we assumed responsibility as successor to Great Western. No additional compensation may be deferred under this plan. Interest accrues on fund balances outstanding within the plan at enhanced rates. In accordance with applicable SEC regulations, the reported above-market interest consists of earnings to the extent the interest rate exceeded 120% of the applicable federal long-term rate (the "*Benchmark Rate*"). Mr. Frank's enhanced rate for 2007 was 6.31%, which exceeded the Benchmark Rate of 6.27%.

(5)

For Mr. Frank, this column includes certain retirement benefits to which he is entitled under an unfunded directors' retirement plan for which our Company assumed responsibility as successor to Great Western Financial Corporation. Upon termination of service on Great Western's board of directors, each eligible director became entitled under the plan to an annual retirement benefit equal to the sum of the annual retainer previously paid to members of the Great Western board plus 12 times the monthly meeting fee, both as in effect at the time of the director's termination. Benefits are payable for a period equal to the number of years that the eligible director served as a Great Western director and will be provided to the surviving spouse or other designated beneficiary following an eligible director's death. Pursuant to the plan, Mr. Frank is entitled to receive quarterly payments of \$11,650. Mr. Frank is entitled to receive these payments until October 2008.

**PART IV**

**Exhibits**

(b)

Exhibits:

The exhibits filed as part of this report and exhibits incorporated herein by reference to other documents are listed in the Index of Exhibits to this Annual Report on Form 10-K (pages E-1 through E-5).

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on May 22, 2008.

**WASHINGTON MUTUAL, INC.**

/s/ THOMAS W. CASEY

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Thomas W. Casey  
*Executive Vice President and Chief Financial Officer (Principal  
Financial Officer)*

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**WASHINGTON MUTUAL, INC.  
INDEX OF EXHIBITS  
DESCRIPTION**

<b>EXHIBIT NUMBER</b>	<b>DESCRIPTION</b>
3.1	Amended and Restated Articles of Incorporation of the Company, as amended on January 22, 2001, February 8, 2001, June 22, 2006, September 15, 2006, December 12, 2006, May 23, 2007 and December 17, 2007. (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2007, File No. 1-14667 (the "2007 10-K")).
3.2	Restated Bylaws of the Company, as amended (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2006, File No. 1-14667 (the "2006 10-K")).
4.1	Rights Agreement dated December 20, 2000 between Washington Mutual, Inc. and Mellon Investor Services, LLC (Incorporated by reference to the Company's Current Report on Form 8-K filed January 8, 2001, File No. 0-25188).
4.2	The registrant will furnish upon request copies of all instruments defining the rights of holders of long-term debt instruments of registrant and its consolidated subsidiaries.
4.3	Warrant Agreement dated as of April 30, 2001 (Incorporated by reference to the Company's Registration Statement on Form S-3, File No. 333-63976).
4.4	2003 Amended and Restated Warrant Agreement dated March 11, 2003 by and between Washington Mutual, Inc. and Mellon Investor Services LLC, as Warrant Agent (Incorporated by reference to the Company's Current Report on Form 8-K dated March 12, 2003, File No. 1-14667).
4.5	Second Supplemental Indenture between Washington Mutual, Inc. and The Bank of New York, as Senior Trustee, dated November 20, 2002 (Incorporated by reference to the Company's Current Report on Form 8-K filed November 25, 2002).
4.6	First Supplemental indenture between Washington Mutual, Inc. and The Bank of New York, as Senior Trustee, dated August 1, 2002 (Incorporated by reference to the Company's Current Report on Form 8-K filed November 25, 2002).
4.7	Second Supplemental Indenture between Washington Mutual, Inc. and The Bank of New York, as Subordinated Trustee, dated March 16, 2004 (Incorporated by reference to the Company's Current Report on Form 8-K filed March 24, 2004).
4.8	First Supplemental Indenture between Washington Mutual, Inc. and The Bank of New York, as Subordinated Trustee, dated August 1, 2002 (Incorporated by reference to the form of First Supplemental Indenture filed with the Company's Registration Statement on Form S-3 filed April 18, 2002, File No. 333-86546).
4.9	Washington Mutual, Inc.'s Standard Multiple-Series Indenture Provisions dated August 1, 2002 (Incorporated by reference to the Company's Current Report on Form 8-K filed November 25, 2002).

**Management Contracts and Compensatory Plans and Arrangements (Exhibits 10.1-10.24)**

- 10.1 Washington Mutual, Inc. 2003 Equity Incentive Plan (the "EIP") (Incorporated by reference to the Company's Annual Report on Form 10-K/A for the year ended December 31, 2003 (the "2003 10-K/A"), as amended by (i) an Amendment No. 1 to the EIP (Incorporated by reference to the 2003 10-K/A), including (ii) a Form of the EIP Stock Option Agreement (1-Year Cliff Vesting) (Incorporated by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (the "3Q 2004 10-Q"), (iii) a Form of the EIP Stock Option Agreement (3-Year Graded Vesting) (Incorporated by reference to the 3Q 2004 10-Q), (iv) a Form of the EIP Notice of Stock Option Grant (Incorporated by reference to the 3Q 2004 10-Q), (v) a Form of the EIP Restricted Stock Award Agreement (3-Year Cliff Vesting) (Incorporated by reference to the 3Q 2004 10-Q), (vi) a Form of the EIP Restricted Stock Award Agreement (3-Year Graduated Vesting) (Incorporated by reference to the 3Q 2004 10-Q), (vii) a Form of the EIP Performance Share Award Agreement (Incorporated by reference to the 3Q 2004 10-Q), (viii) Form of the EIP Restricted Stock Award Agreement (Incorporated by reference to the Company's Current Report on Form 8-K dated January 18, 2005, File No. 1-14667), (ix) Form of EIP Stock Option Agreement (3-Year Graded Vesting) (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ending December 31, 2004 (the "2004 10-K"), File No. 1-14667), and (x) Form of EIP Stock Option Agreement (1-Year Cliff Vesting Nonqualified Options) (Incorporated by reference to the 2004 10-K).
- 10.2 Washington Mutual, Inc. Amended and Restated 2003 Equity Incentive Plan (the "Restated EIP") (Incorporated by reference to the Company's Definitive Proxy Statement on Form 14A filed March 17, 2006 (the "2006 Proxy"), File No. 1-14667), as amended by (i) an Amendment No. 1 to the Restated EIP (Incorporated by reference to the 2006 10-K), including (ii) a Form of EIP Stock Option Agreement (3-Year, Price Vesting) (Incorporated by reference to the 2007 10-K), (iii) a Form of the EIP Stock Option Agreement (4-Year, Price Vesting) (Incorporated by reference to the 2007 10-K), (iv) a Form of the EIP Restricted Stock Award Agreement (3-Year, Performance Vesting) (Incorporated by reference to the 2007 10-K), and (v) a Form of the EIP Restricted Stock Award Agreement (3-Year Vesting) (Incorporated by reference to the 2007 10-K).
- 10.3 Form of Cash Long Term Incentive Award (Incorporated by reference to the 2007 10-K).
- 10.4 Washington Mutual, Inc. Executive Incentive Compensation Plan (Incorporated by reference to the 2006 Proxy).
- 10.5 Washington Mutual 1994 Stock Option Plan as amended and restated as of February 15, 2000 (the "1994 Stock Option Plan") (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2000 (the "2000 10-K"), File No. 1-14667), as amended by (i) a First Amendment to the 1994 Stock Option Plan (Incorporated by reference to the 2000 10-K), and (ii) a Second Amendment to the 1994 Stock Option Plan (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2001 (the "2001 10-K"), File No. 1-14667).
- 10.6 Washington Mutual Equity Incentive Plan (formerly known as Washington Mutual Restricted Stock Plan) as amended and restated as of January 16, 2001 (Incorporated by reference to the 2001 10-K).

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- 10.7 Amended and Restated 2002 Employee Stock Purchase Plan (the "ESPP") (Incorporated by reference to the 2003 10-K/A), as amended by (i) an Amendment No. 1 to the ESPP (Incorporated by reference to the 2003 10-K/A), and (ii) an Amendment No. 2 to the ESPP (Incorporated by reference to the 2003 10-K/A).
- 10.8 WaMu Savings Plan as amended and restated effective January 1, 2006 (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2005 (the "2005 10-K"), File No. 1-14667), as amended by (i) an Amendment No. 1 to the WaMu Savings Plan (Incorporated by reference to the 2006 10-K), (ii) an Amendment No. 2 to the WaMu Savings Plan (Incorporated by reference to the 2006 10-K), (iii) an Amendment No. 3 to the WaMu Savings Plan (Incorporated by reference to the 2007 10-K), and (iv) an Amendment No. 4 to the WaMu Savings Plan (Incorporated by reference to the 2007 10-K).
- 10.9 Washington Mutual, Inc. Supplemental Employees' Retirement Plan, amended and restated effective July 20, 2004 (the "SERP") (Incorporated by reference to the 2005 10-K), as amended by (i) an Amendment No. 1 to the SERP (Incorporated by reference to the 2005 10-K), and (ii) an Amendment No. 2 to the SERP (Incorporated by reference to the 2006 10-K).
- 10.10 Washington Mutual, Inc. Supplemental Executive Retirement Accumulation Plan, amended and restated effective January 1, 2004 (the "SERAP") (Incorporated by reference to the 2005 10-K), as amended by (i) an Amendment No. 1 to the SERAP (Incorporated by reference to the 2005 10-K), and (ii) an Amendment No. 2 to the SERAP (Incorporated by reference to the 2006 10-K).
- 10.11 Washington Mutual, Inc. Deferred Compensation Plan (the "DCP"), amended and restated effective July 20, 2004 (Incorporated by reference to the 2004 10-K), as amended by (i) an Amendment No. 1 to the DCP (Incorporated by reference to the 2005 10-K), (ii) an Amendment No. 2 to the DCP (Incorporated by reference to the 2005 10-K), (iii) an Amendment No. 3 to the DCP (Incorporated by reference to the 2007 10-K), (iv) an Amendment No. 4 to the DCP (Incorporated by reference to the 2006 10-K), and (v) an Amendment No. 5 to the DCP (Incorporated by reference to the Company's Current Form 8-K filed November 15, 2007, File No. 1-14667).
- 10.12 Washington Mutual, Inc. Executive Target Retirement Income Plan (the "ETRIP"), effective January 1, 2004 (Incorporated by reference to the 2004 10-K).
- 10.13 Great Western Financial Corporation Directors' Deferred Compensation Plan (1992 Restatement) (Incorporated by reference to Great Western's Annual Report on Form 10-K for the year ended December 31, 1991, File No. 001-04075), as amended by (i) an Amendment to Great Western Financial Corporation Directors' Senior Officers' and basic Deferred Compensation Plans (1992 Restatement) (Incorporated by reference to Great Western's Annual Report on Form 10-K for the year ended December 31, 1994, File No. 001-04075), (ii) an Amendment No. 2 to Directors' Deferred Compensation Plan (1992 Restatement) (Incorporated by reference to Great Western's Quarterly Report on Form 10-Q for the quarter ended March 31, 1996, File No. 001-04075), and (iii) an Amendment No. 1996-2 to Directors' Deferred Compensation Plan, dated December 10, 1996 (Incorporated by reference to Great Western's 1996 10-K).

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- 10.14 Omnibus Amendment 1997-1 amending the definition of change in control in the Great Western Financial Corporation 1988 Stock Option and Incentive Plan, as amended December 10, 1996, the Great Western Financial Corporation Directors' Deferred Compensation Plan (1992 Restatement), as amended December 10, 1996, and the Employee Home Loan Program (revised and restated as of April 27, 1993), as amended December 10, 1996 (Incorporated by reference to Great Western's 1996 10-K).
- 10.15 H.F. Ahmanson & Company 1988 Director's Stock Incentive Plan, as amended (Incorporated by reference to H.F. Ahmanson & Company's Annual Report on Form 10-K for the year ended December 31, 1989, File No. 1-08930).
- 10.16 H.F. Ahmanson & Company 1996 Nonemployee Directors' Stock Incentive Plan (Incorporated by reference to H.F. Ahmanson & Company's Annual Report on Form 10-K for the year ended December 31, 1995, File No. 1-08930).
- 10.17 Dime Voluntary Deferred Compensation Plan for Directors (the "Bancorp Director Deferred Compensation Plan"), as amended and restated effective as of July 24, 1997 (Incorporated by reference to Dime's Annual Report on Form 10-K for the year ended December 31, 1997), as amended by (i) an Amendment effective March 26, 1998, to the Bancorp Director Deferred Compensation Plan (Incorporated by reference to Dime's Annual Report on Form 10-K for the year ended December 31, 1998 (the "Dime's 1998 10-K"), (ii) an Amendment effective October 1, 1999, to the Bancorp Director Deferred Compensation Plan (Incorporated by reference to Dime's Annual Report on Form 10-K for the year ended December 31, 1999), and (iii) an Amendment to the Bancorp Director Deferred Compensation Plan effective May 18, 2000 (Incorporated by reference to the 14d-9 Amendment No. 11).
- 10.18 Dime 1997 Stock Incentive Plan for Outside Director's, as amended and restated effective March 27, 1998 (the "1997 Outside Director Plan") (Incorporated by reference to Dime's 1998 10-K), as amended by (i) an Amendment effective as of December 12, 2000 to the 1997 Outside Director Plan (Incorporated by reference to Dime's Annual Report on Form 10-K for the year ended December 31, 2000, File No. 1-13094).
- 10.19 February 2001 WAMU Shares Plan (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2002, File No. 1-14667), as amended by (i) Amendment No. 1 to February 2001 WAMU Shares Plan (Incorporated by reference to the 2003 10-K/A), (ii) Amendment No. 3 to February 2001 WAMU Shares Plan (Incorporated by reference to the 2003 10-K/A), and (iii) Amendments to the January 1999 WAMU Shares Plan and the February 2001 WAMU Shares Plan (collectively, the "Plans") (Incorporated by reference to the 2003 10-K/A).
- 10.20 Employment Agreement of Kerry K. Killinger (Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 1997, (the "1997 10-K"), File No. 0-25188), as amended by (i) a First Amendment to the Employment Agreement, effective as of December 31, 2007 (Incorporated by reference to the Company's Current Report on Form 8-K filed January 7, 2008, File No. 1-14667).
- 10.21 Employment Agreement of Stephen J. Rotella (Incorporated by reference to the Company's Current Report on Form 8-K filed December 27, 2004, File No. 1-14667), as amended by (i) a First Amendment to the Employment Agreement, effective as of December 31, 2007 (Incorporated by reference to the Company's Current Report on Form 8-K filed January 7, 2008, File No. 1-14667).

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- 10.22 Restricted Stock Award Agreement, by and between the Company and Stephen J. Rotella, dated January 10, 2005 (Incorporated by reference to the Company's Current Report on Form 8-K filed January 14, 2005, File No. 1-14667).
- 10.23 Form of Change in Control Agreement executed by Executive Officers other than Melissa J. Ballenger, Stephen J. Rotella and Kerry Killinger (Incorporated by reference to the Company's Current Report on Form 8-K filed January 7, 2008, File No. 1-14667).
- 10.24 Executive Severance and Mutual Release Agreement dated December 10, 2007 by and between the Company and Fay Chapman (Incorporated by reference to the 2007 10-K).
- 12.1 Computation of Ratios of Earnings to Fixed Charges (Incorporated by reference to the 2007 10-K).
- 12.2 Computation of Ratios of Earnings to Fixed Charges and Preferred Dividends (Incorporated by reference to the 2007 10-K).
- 21 List of Subsidiaries of the Registrant (Incorporated by reference to the 2007 10-K).
- 23 Consent of Deloitte & Touche LLP (Incorporated by reference to the 2007 10-K).
- 31.1 Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Filed herewith).
- 31.2 Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Filed herewith).
- 32.1 Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Incorporated by reference to the 2007 10-K).
- 32.2 Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Incorporated by reference to the 2007 10-K).

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