

**Xerox Federal Credit Union**  
**Financial Statements**  
**December 31, 2007**

**McGladrey & Pullen**

Certified Public Accountants

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# McGladrey & Pullen

Certified Public Accountants

## INDEPENDENT AUDITOR'S REPORT

Supervisory Committee  
Xerox Federal Credit Union  
El Segundo, California

We have audited the accompanying statement of financial condition of Xerox Federal Credit Union (a federally chartered Credit Union) as of December 31, 2007 and the related statements of income, comprehensive income, members' equity, and cash flows for the year then ended. These financial statements are the responsibility of the Credit Union's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Xerox Federal Credit Union as of December 31, 2007 and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

*McGladrey & Pullen, LLP*

Los Angeles, California  
June 17, 2008

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**XEROX FEDERAL CREDIT UNION  
STATEMENT OF FINANCIAL CONDITION  
DECEMBER 31, 2007**

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**ASSETS**

Cash and cash equivalents	\$ 33,342,509
Investments	
Available-for-sale	54,733,080
Held-to-maturity	1,989,657
Other	57,811,949
Loans receivable, net	596,870,571
Accrued interest receivable	2,874,314
Property and equipment, net	8,837,527
National Credit Union Share Insurance Fund deposit	4,260,555
Other assets	10,223,328
	<hr/>
	\$ 770,943,490
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**LIABILITIES AND MEMBERS' EQUITY**

Liabilities

Members' shares	\$ 556,520,446
Borrowed funds	107,300,000
State of California Treasury Deposits	10,000,000
Accrued expenses and other liabilities	8,962,156
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Total liabilities 682,782,602

Commitments and contingent liabilities

Members' Equity

Retained earnings, substantially restricted	88,282,956
Accumulated other comprehensive income	(122,068)
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Total members' equity 88,160,888

\$ 770,943,490

**XEROX FEDERAL CREDIT UNION  
STATEMENT OF INCOME  
FOR THE YEAR ENDED DECEMBER 31, 2007**

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**INTEREST INCOME**

Interest on loans receivable	\$ 37,049,820
Interest on investments and cash equivalents	6,895,844

43,945,664

**INTEREST EXPENSE**

Dividends on members' shares	16,439,601
Interest on borrowed funds and state of California treasury deposits	4,811,419

21,251,020

**NET INTEREST INCOME**

22,694,644

**PROVISION FOR LOAN LOSSES**

2,518,980

**NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES**

20,175,664

**NON-INTEREST INCOME**

Service charges and other fees	5,285,732
Debit card interchange income	1,589,214
Rental income	1,486,779
Other non-interest income	470,748

8,832,473

**GENERAL AND ADMINISTRATIVE EXPENSES**

Salaries and benefits	17,388,844
Operations	13,574,153
Occupancy	1,576,160

32,539,157

**NET LOSS**

\$ (3,531,020)

**XEROX FEDERAL CREDIT UNION  
STATEMENT OF COMPREHENSIVE INCOME  
FOR THE YEAR ENDED DECEMBER 31, 2007**

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<b>NET LOSS</b>	\$ (3,531,020)
<b>OTHER COMPREHENSIVE INCOME</b>	
Unrealized holding gains on investments classified as available-for-sale	<u>1,281,146</u>
<b>COMPREHENSIVE LOSS</b>	<u><u>\$ (2,249,874)</u></u>

**XEROX FEDERAL CREDIT UNION  
STATEMENT OF MEMBERS' EQUITY  
FOR THE YEAR ENDED DECEMBER 31, 2007**

	<u>Retained Earnings</u>			<u>Accumulated Other Comprehensive Income</u>
	<u>Regular Reserve</u>	<u>Unappropriated</u>	<u>Total</u>	
Balance, December 31, 2006, as restated, see Note 14	\$ 20,183,596	\$ 71,630,380	\$ 91,813,976	\$ (1,403,214)
Net loss		(3,531,020)	(3,531,020)	
Net change in unrealized gains (losses) on available- for-sale investments				1,281,146
Balance, December 31, 2007	<u>\$ 20,183,596</u>	<u>\$ 68,099,360</u>	<u>\$ 88,282,956</u>	<u>\$ (122,068)</u>

**XEROX FEDERAL CREDIT UNION  
STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2007**

**OPERATING ACTIVITIES**

Net loss	\$ (3,531,020)
Adjustments to reconcile net income to net cash provided by operating activities:	
Amortization of securities	91,190
Provision for loan losses	2,518,980
Depreciation and amortization	1,952,418
Net change in:	
Accrued interest receivable	392,536
Other assets	(2,520,111)
Accrued expenses and other liabilities	1,776,366
	680,359
Net cash provided by operating activities	680,359

**INVESTING ACTIVITIES**

Purchases of available-for-sale investments	(1,996,668)
Proceeds from maturities of available-for-sale investments	10,796,719
Proceeds from maturities of held-to-maturity investments	1,876,381
Net decrease in other investments	10,092,628
Net increase in loans receivable	(19,049,806)
Increase in the National Credit Union Share Insurance Fund deposit	645,168
Purchases of property and equipment	(3,848,994)
	(1,484,572)
Net cash used in investing activities	(1,484,572)

**FINANCING ACTIVITIES**

Net increase in borrowed funds	54,000,000
Repayments of State of California Treasury deposits	(47,000,000)
Net decrease in members' shares	(30,686,365)
	(23,686,365)
Net cash used in financing activities	(23,686,365)

<b>DECREASE IN CASH AND CASH EQUIVALENTS</b>	(24,490,578)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR, AS RESTATED, SEE NOTE 14</b>	57,833,087
	57,833,087

<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>\$ 33,342,509</b>
	\$ 33,342,509

**SUPPLEMENTAL CASH FLOW INFORMATION**

Dividends paid on members' shares and interest paid on borrowed funds and state of California treasury deposits	\$ 21,375,132
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**XEROX FEDERAL CREDIT UNION  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2007**

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**1. SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations:** Xerox Federal Credit Union (the Credit Union) is a cooperative association holding a corporate charter under the provisions of the Federal Credit Union Act. Participation in the Credit Union is limited to those individuals that qualify for membership, including employees and family members of employees of Xerox Corporation. The field of membership is defined in the Credit Union's Charter and Bylaws. Effective April 2008, the credit union changed its name from Xerox Federal Credit Union to Xceed Federal Credit Union.

**Use of Estimates:** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. A material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for loan losses.

**Concentrations of Credit Risk:** A significant amount of the Credit Union's business activity is with its members who are employed by Xerox Corporation. The Credit Union may be exposed to credit risk from a regional economic standpoint, since a significant concentration of its borrowers work or reside in California and New York.

**Cash and Cash Equivalents:** For the purpose of the statement of financial condition and the statement of cash flows, cash and cash equivalents includes cash on hand, amounts due from financial institutions, and highly liquid debt instruments classified as cash which were purchased with maturities of three months or less. Amounts due from financial institutions may, at times, exceed federally insured limits.

**Investments:** Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as "available for sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of individual available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In determining whether other-than-temporary impairment exists, management considers many factors, including (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Credit Union to retain its investment in the issue for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Other investments are classified separately and are stated at cost.

**Federal Home Loan Bank Stock:** The Credit Union, as a member of the Federal Home Loan Bank (FHLB) system, is required to maintain an investment in capital stock of the FHLB in an amount equal to the greater of 1% of its outstanding mortgage loans or 5% of advances from the FHLB. No ready market exists for the FHLB stock, and it has no quoted market value.

**XEROX FEDERAL CREDIT UNION  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2007**

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**Loans Receivable:** The Credit Union grants mortgage, commercial and consumer loans receivable. The ability of the members to honor their contracts is dependent upon the real estate and general economic conditions of the area.

Loans that the Credit Union has the intent and ability to hold for the foreseeable future or until maturity or pay-off are stated at their outstanding unpaid principal balances, less an allowance for loan losses and net deferred origination fees and costs. Interest income on loans is recognized over the term of the loan and is calculated using the simple interest method on principal amounts outstanding.

The accrual of interest income on loans is discontinued at the time the loan is 60 days past due, unless the credit is well secured and in the process of collection. Other personal loans are typically charged off no later than 180 days past due. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if the collection of principal and interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all of the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Loan fees and certain direct loan origination costs are deferred, and the net cost is recognized as an adjustment to interest income using the interest method over the contractual life of the loans, adjusted for estimated prepayments based on the Credit Union's historical prepayment experience.

**Allowance for Loan Losses:** The allowance for loan losses is established as losses are estimated to have occurred though a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is likely. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of the underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available. In addition, regulatory agencies, as an integral part of their examination process, periodically review the Credit Union's allowance for loan losses, and may require the Credit Union to make additions to the allowance based on their judgment about information available to them at the time of their examinations.

The Credit Union's allowance for loan losses is that amount considered adequate to absorb probable losses in the portfolio based on management's evaluations of the size and current risk characteristics of the loan portfolio. Such evaluations consider prior loss experience, the risk rating and the levels of non-performing loans. Specific allowances for loan losses are established for large impaired loans on an individual basis as required per SFAS No. 114, *Accounting by Creditors for Impairment of a Loan*. The specific allowances established for these loans are based on a thorough analysis of the most probable source of repayment, including the present value of the loan's expected future cash flow, the loan's estimated market value, or the estimated fair value of the underlying collateral. General allowances are established for loans that can be grouped into pools based on

**XEROX FEDERAL CREDIT UNION  
NOTES TO FINANCIAL STATEMENTS  
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similar characteristics as described in SFAS No. 5, *Accounting for Contingencies*. In this process, general allowance factors are based on an analysis of historical charge-off experience and expected losses given default derived from the Credit Union's internal risk rating process. These factors are developed and applied to the portfolio by loan type. The qualitative factors associated with the allowances are subjective and require a high degree of management judgment. These factors include the credit quality statistics, recent economic uncertainty, losses incurred from recent events, and lagging data.

**Property and Equipment:** Land is carried at cost. Building, leasehold improvements, and furniture and equipment are carried at cost, less accumulated depreciation and amortization. Buildings and furniture and equipment are depreciated using the straight-line method over the estimated useful lives of the assets. The cost of leasehold improvements is amortized using the straight-line method over the terms of the related leases.

**Transfers of Financial Assets:** Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Credit Union, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Credit Union does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

**National Credit Union Share Insurance Fund Deposit:** The deposit in the National Credit Union Share Insurance Fund (NCUSIF) is in accordance with National Credit Union Administration (NCUA) regulations, which require the maintenance of a deposit by each federally insured Credit Union in an amount equal to 1% of its insured members' shares. The deposit would be refunded to the Credit Union if its insurance coverage is terminated, if it converts its insurance coverage to another source, or if management of the fund is transferred from the NCUA Board.

**NCUSIF Insurance Premium:** The Credit Union is required to pay an annual insurance premium equal to one-twelfth of one percent of total insured shares, unless the payment is waived or reduced by the NCUA Board. The NCUA Board waived the 2007 insurance premiums.

**Members' Shares:** Members' shares are the savings deposit accounts of the owners of the Credit Union. Share ownership entitles the members to vote in the annual elections of the Board of Directors and on other corporate matters. Irrespective of the amount of shares owned, no member has more than one vote. Members' shares are subordinated to all other liabilities of the Credit Union upon liquidation. Dividends on members' shares are based on available earnings at the end of a dividend period and are not guaranteed by the Credit Union. Dividend rates are set by the Credit Union's Board of Directors.

**Advertising Costs:** Advertising costs are expensed as incurred.

**Income Taxes:** The Credit Union is exempt, by statute, from federal and state income taxes.

**Comprehensive Income:** Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the members' equity section of the statements of financial condition. For 2007, other comprehensive income includes no reclassification adjustments.

**XEROX FEDERAL CREDIT UNION  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2007**

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**Recent Accounting Pronouncements:** In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurement. SFAS No. 157 also emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and sets out a fair value hierarchy with the highest priority being quoted prices in active markets. Under SFAS No. 157, fair value measurements are disclosed by level within that hierarchy. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, except for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis for which delayed application is permitted until fiscal years beginning after November 15, 2008. The Credit Union is currently assessing the potential effect of SFAS No. 157 on its financial position, results of operations and cash flows.

In February 2007, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ("SFAS No. 159"). SFAS No. 159 permits companies to elect to follow fair value accounting for certain financial assets and liabilities in an effort to mitigate volatility in earnings without having to apply complex hedge accounting provisions. The standard also establishes presentation and disclosure requirements designed to facilitate comparison between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Credit Union is currently evaluating the impact of the adoption of SFAS No. 159 on its financial position, results of operations and cash flows.

In December 2007, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141R, *Business Combinations*. This new standard significantly changes the accounting for business combination transactions as the pooling-of-interests accounting method will no longer be an acceptable accounting method. This change is effective for fiscal years beginning on or after December 15, 2008, with early adoption prohibited. The Credit Union is currently evaluating the future impact of FASB 141R on its financial position, results of operations and cash flows.

**2. INVESTMENTS**

Investments classified as available-for-sale consist of the following at December 31, 2007:

	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Federal agencies securities	\$ 41,520,791	\$ 105,938	\$ (130,642)	\$ 41,496,087
Mortgage-backed securities	13,334,357	92,230	(189,594)	13,236,993
	<u>\$ 54,855,148</u>	<u>\$ 198,168</u>	<u>\$ (320,236)</u>	<u>\$ 54,733,080</u>

Investments classified as held-to-maturity consist of the following at December 31, 2007:

	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Mortgage-backed securities	\$ 1,989,657	\$ 1,392	\$ (32,397)	\$ 1,958,652

**XEROX FEDERAL CREDIT UNION  
NOTES TO FINANCIAL STATEMENTS  
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Securities totaling \$31,092,583 have been pledged as collateral to secure State of California Treasury Deposits as disclosed in Note 9.

Securities totaling \$15,337,127 have been pledged as collateral to secure Federal Home Loan Bank advances as more fully disclosed in Note 8.

Investments by maturity as of December 31, 2007 are summarized as follows:

	Available-for-sale		Held-to-maturity		Other
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	
No contractual maturity	\$ 0	\$ 0	\$ 0	\$ 0	\$ 10,286,720
Less than 1 year maturity	19,979,504	19,926,562	0	0	11,423,639
1 – 5 years maturity	21,541,287	21,569,525	0	0	30,320,475
5 – 10 years maturity	0	0	0	0	5,781,115
Mortgage-backed securities	13,334,357	13,236,993	1,989,657	1,958,652	0
	<u>\$ 54,855,148</u>	<u>\$ 54,733,080</u>	<u>\$ 1,989,657</u>	<u>\$ 1,958,652</u>	<u>\$ 57,811,949</u>

Expected maturities of mortgage-backed securities may differ from contractual maturities because borrowers may have the right to call or prepay the obligations and are, therefore, classified separately with no specific maturity date. FHLB stock and member and permanent capital accounts have been classified with no contractual maturity.

Gross unrealized losses and fair value by length of time that the individual securities have been in a continuous unrealized loss position at December 31, 2007 are as follows:

Available-for-sale	Fair Value	Continuous Unrealized Losses Existing For:		Total Unrealized Losses
		Less Than 12 Months	More Than 12 Months	
Federal agencies securities	\$ 19,929,688	\$ 0	\$ (130,642)	\$ (130,642)
Mortgage-backed securities	8,815,810	(2,868)	(186,726)	(189,594)
	<u>\$ 28,745,498</u>	<u>\$ (2,868)</u>	<u>\$ (317,368)</u>	<u>\$ (320,236)</u>
<b>Held-to-maturity</b>				
Mortgage-backed securities	<u>\$ 1,758,456</u>	<u>\$ 0</u>	<u>\$ (32,397)</u>	<u>\$ (32,397)</u>

At December 31, 2007, the investment portfolio included 30 securities, 27 of which have current unrealized losses which have existed for longer than one year. All of these securities are considered to be acceptable credit risks. Based upon an evaluation of the available evidence, including recent changes in market rates, credit rating information and information obtained from regulatory filings, management believes the decline in fair value for these securities is temporary. In addition, the Credit Union has the intent and ability to hold these investment securities for a period of time sufficient to allow for an anticipated recovery.

**XEROX FEDERAL CREDIT UNION  
NOTES TO FINANCIAL STATEMENTS  
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Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period in which the other-than-temporary impairment is identified.

Other investments consist of the following at December 31, 2007:

Share certificates in a corporate credit union	\$ 47,425,229
Certificates of deposit in banks and savings institutions	100,000
Member capital account in a corporate credit union	2,743,620
FHLB stock	5,043,100
Permanent capital account in a corporate credit union	2,500,000
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	\$ 57,811,949
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Certificates are generally non-negotiable and non-transferable, and may incur substantial penalties for withdrawal prior to maturity.

Permanent capital accounts are uninsured equity capital accounts and are redeemable only if called by the corporate credit union. Member capital accounts are uninsured equity capital accounts that may be redeemed with a three-year notice. The fair value of other investments approximates book value.

**3. LOANS RECEIVABLE**

Loans receivable consist of the following at December 31, 2007:

Mortgage loans:	
Fixed rate	\$ 226,646,686
Hybrid	21,097,414
Home equity line of credit, variable rate	106,134,213
Commercial real estate	2,664,073
Participation loans purchased	13,429,432
	<hr/>
	369,971,818
Vehicle loans	178,414,167
Other consumer loans, primarily unsecured	49,358,526
Other commercial loans, primarily unsecured	236,927
	<hr/>
	597,981,438
Deferred net loan origination costs	1,811,990
Allowance for loan losses	(2,922,857)
	<hr/>
	\$ 596,870,571
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The participation loans purchased consist of pools of residential mortgage loans purchased without recourse. The lead lender is responsible for the administration of these loans, including the collection of payments, record

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NOTES TO FINANCIAL STATEMENTS  
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keeping, and collection procedures, if necessary. The Credit Union holds a fractional security interest in the underlying collateral.

Mortgage loans totaling \$341,936,000 have been pledged as collateral to secure amounts borrowed from the Federal Home Loan Bank as disclosed in Note 8.

Vehicle loans totaling \$178,414,000 have been pledged as collateral to secure amounts borrowed from a corporate credit union as disclosed in Note 8.

Mortgage loans totaling \$52,582,000 have been pledged as collateral to secure State of California Treasury deposits as disclosed in Note 9.

The following is an analysis of the allowance for loan losses for the year ended December 31, 2007:

Balance, beginning of year, as restated, see Note 14	\$ 2,682,835
Provision for loan losses	2,518,980
Recoveries	282,154
Loans charged off	(2,561,112)
	\$ 2,922,857
	\$ 2,922,857

**4. LOAN SERVICING**

Loans serviced for others are not included in the accompanying statements of financial condition. The unpaid principal balances of these loans at December 31, 2007 are summarized as follows:

Mortgage loan portfolios serviced for:	
Other investors	\$ 11,360,087
Freddie Mac	11,053,551
	\$ 22,413,638
Automobile loan portfolios serviced for others:	
3.5% limited subordination	\$ 14,621,556
4.25% limited subordination	1,950,640
No recourse	20,714,984
	\$ 37,287,180
	\$ 37,287,180

Automobile loans with limited subordination consist of pools of loans sold to other credit unions with limited recourse. Net loan losses in each pool will be charged first to the subordination amount held by the Credit Union.

**XEROX FEDERAL CREDIT UNION  
NOTES TO FINANCIAL STATEMENTS  
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**5. PROPERTY AND EQUIPMENT**

Property and equipment at December 31, 2007 are summarized as follows:

Land	\$	323,886
Building		4,654,759
Leasehold improvements		1,841,450
Furniture and equipment		16,363,328
Construction in progress		2,719,575
		25,902,998
Accumulated depreciation and amortization		(17,065,471)
		\$ 8,837,527

Construction in progress consists of numerous branch remodels, new headquarters construction and various other projects. Upon completion, the fixed asset will be allocated to the appropriate account. Remaining commitments on the projects total \$14,660,000. The credit union has also entered into a commitment during 2007 to purchase a piece of land in New York for a total purchase price of \$1,300,000.

The Credit Union leases 16 offices. The operating leases contain renewal options and provisions requiring the Credit Union to pay property taxes and operating expenses over base period amounts. All rental payments are dependent only upon the lapse of time. Minimum rental payments under operating leases with initial or remaining terms of one year or more at December 31, 2007 are as follows:

<u>Years Ending December 31</u>		
2008	\$	849,000
2009		917,000
2010		860,000
2011		769,000
2012		637,000
Subsequent years		4,492,000
		\$ 8,524,000

Rental expense for the years ended December 31, 2007 for all facilities leased under operating leases totaled \$647,700.

**6. OTHER ASSETS**

Included in other assets are variable universal life insurance policies totaling approximately \$8,355,230 as of December 31, 2007. The Credit Union is the owner and beneficiary of these policies. The policies provide for investments in various unit investment trusts administered by Lincoln Financial and Pacific Life. These investments are accounted for at fair value which equals cash surrender value. These investments incurred a gain of approximately \$106,000 for the year ended December 31, 2007, which is included in other non-interest income.

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**7. MEMBERS' SHARES**

Members' shares are summarized as follows as of December 31, 2007:

Regular shares	\$ 75,632,867
Share draft accounts	93,277,684
Money market accounts	151,660,358
Individual retirement accounts	7,151,011
Certificates	<u>228,762,530</u>
	556,484,450
Dividends payable	<u>35,996</u>
	<u>\$ 556,520,446</u>

Shares by maturity as of December 31, 2007 are summarized as follows:

No contractual maturity	\$ 327,721,920
0 – 1 year maturity	164,673,908
1 – 2 years maturity	44,625,936
2 – 3 years maturity	8,613,544
3 – 4 years maturity	1,909,479
4 – 5 years maturity	<u>8,939,663</u>
	<u>\$ 556,484,450</u>

Regular shares, share draft accounts, money market accounts, and individual retirement account shares have no contractual maturity. Certificate accounts have maturities of 5 years or less.

The National Credit Union Share Insurance Fund insures members' shares up to \$100,000, and certain individual retirement and Keogh accounts up to \$250,000.

The aggregate amount of certificates in denominations of \$100,000 or more at December 31, 2007 is approximately \$76,928,000.

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**8. BORROWED FUNDS**

The Credit Union utilizes a demand loan agreement with the Federal Home Loan Bank (FHLB). The terms of the agreement call for pledging certain investments held in safekeeping by the FHLB and a portion of the Credit Union's mortgage loan portfolio. The agreement provides for a maximum borrowing capacity of \$175,612,135. As of December 31, 2007 the advances total \$107,300,000 with maturities as follows:

	<u>Balance</u>	<u>Weighted Cost</u>
0 – 1 year maturity	\$ 0	0%
2 – 3 years maturity	50,000,000	3.9%
3 – 4 years maturity	45,000,000	4.1%
4 – 5 years maturity	2,300,000	5.1%
Over 5 years maturity	10,000,000	4.4%
	<u>\$ 107,300,000</u>	<u>4.1%</u>

The Credit Union also utilizes a secured borrowing agreement with a corporate credit union. This agreement calls for the pledging of vehicle loans as security for any and all obligations taken by the Credit Union under this agreement. The agreement provides for a credit limit of \$85 million with interest charged at a rate determined by the lender on a periodic basis. At December 31, 2007 there was no outstanding balance under this agreement. The agreement is reviewed for continuation by the lender and the Credit Union annually.

The Credit Union also utilizes demand loan agreements with several corporate credit unions. The terms of these agreements call for the pledging of all assets, except for those assets already pledged as collateral under other agreements, as security for any and all obligations taken by the Credit Union under these agreements. The agreements provide for a total credit limit of \$38.7 million with interest charged at rates determined by the lenders on a periodic basis. At December 31, 2007 there were no outstanding balances under these agreements. The agreements are reviewed for continuation by the lenders and the Credit Union annually.

**9. STATE OF CALIFORNIA TREASURY DEPOSITS**

The Credit Union has entered into an agreement with the Treasurer of the State of California whereby the State will deposit funds with the Credit Union. Interest on these deposits will be paid at the end of each calendar quarter and at maturity. The terms of the agreement call for pledging certain investments held in safekeeping at the Federal Reserve Bank and a portion of the Credit Union's mortgage loan portfolio. As of December 31, 2007 the deposits total \$10,000,000 with a maturity date of January 9, 2008.

**10. OFF-BALANCE SHEET ACTIVITIES**

The Credit Union is party to conditional commitments to lend funds in the normal course of business to meet the financing needs of its members. These commitments represent financial instruments to extend credit which include lines of credit, credit cards and home equity lines that involve, to varying degrees, elements of credit and interest rate risk in excess of amounts recognized in the financial statements.

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The Credit Union's exposure to credit loss is represented by the contractual amount of these commitments. The Credit Union follows the same credit policies in making commitments as it does for those loans recorded in the financial statements.

Outstanding loan commitments at December 31, 2007 total approximately \$706,000.

Unfunded loan commitments under lines of credit as of December 31, 2007 are summarized as follows:

Home equity	\$ 111,834,000
Overdraft privilege program	96,600,000
Other consumer	<u>66,364,000</u>
	<u>\$ 274,798,000</u>

Commitments to extend credit are agreements to lend to a member as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Because many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Credit Union evaluates each member's credit worthiness on a case-by-case basis. The amount of collateral obtained to secure borrowing on the lines of credit is based on management's credit evaluation of the member.

**11. COMMITMENTS AND CONTINGENT LIABILITIES**

The Credit Union is a party to various legal actions normally associated with collections of loans and other business activities of financial institutions, the aggregate effect of which, in management's opinion, would not have a material adverse effect on the financial condition or results of operations of the Credit Union.

**12. EMPLOYEE BENEFITS**

The Credit Union employees are participants in numerous benefit and pension plans of Xerox Corporation (the company). All expenses related to payroll and benefits are paid by the company and reimbursed by the Credit Union to the company in the following month. Since the Credit Union employees are only fractional participants in these plans, it is not practical to disclose benefit data.

The Credit Union has entered into deferred compensation agreements with members of the executive management team that provides benefits payable to these employees if they remain employed by the Credit Union until the age specified in the individual contracts. If these employees become fully disabled as defined in the agreement, accrued benefits are immediately payable. The benefits are subject to forfeiture if employment is terminated for cause as defined in the agreement. The estimated liability under the agreements is being accrued over the remaining years until the eligible employees attain the ages specified in the individual contracts. As of December 31, 2007 the total accrued liability is approximately \$1,273,000.

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13. **MEMBERS' EQUITY**

The Credit Union is subject to various regulatory capital requirements administered by the NCUA. Failure to meet minimum capital requirements can initiate certain mandatory – and possibly additional discretionary – actions by regulators that, if undertaken, could have a direct material effect on the Credit Union's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Credit Union must meet specific capital guidelines that involve quantitative measures of the Credit Union's assets, liabilities, and certain off-balance-sheet items as calculated under generally accepted accounting principles. The Credit Union's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Credit Union to maintain minimum amounts and ratios (set forth in the table below) of net worth to total assets. Further, credit unions over \$10,000,000 in assets are also required to calculate a Risk-Based Net Worth (RBNW) requirement which establishes whether or not the Credit Union will be considered "complex" under the regulatory framework. The Credit Union's RBNW requirement as of December 31, 2007 was 6.7%. The minimum requirement to be considered "complex" under the regulatory framework is 6%. Management believes, as of December 31, 2007, that the Credit Union meets all capital adequacy requirements to which it is subject.

As of December 31, 2007, the most recent call reporting period, the NCUA categorized the Credit Union as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," the Credit Union must maintain a minimum net worth ratio of 7% of assets. There are no conditions or events since that notification that management believes have changed the institution's category.

The Credit Union's actual capital amounts and ratios as of December 31, 2007 are presented in the following table:

	<b><u>Amount</u></b>	<b><u>Ratio/Requirement</u></b>
➤ Amount needed to be classified as "adequately capitalized"	\$51,653,214	6.7%
➤ Amount needed to be classified as "well capitalized"	\$53,966,044	7.0%
➤ Actual net worth	\$88,282,956	11.5%

Because the RBNW requirement is less than the net worth ratio, the Credit Union retains its original category. Further, in performing its calculation of total assets, the Credit Union used the quarter-end balance option, as permitted by regulation.

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**14. BUSINESS COMBINATION**

On December 1, 2007, the Credit Union merged with Tiger Federal Credit Union. The merger was accounted for as a pooling of interests and accordingly, all prior year financial statements have been restated to include Tiger Federal Credit Union. The results of operations and applicable account balances of the separate entity for periods prior to the combination are as follows:

	<u>Unaudited November 30, 2007</u>	<u>Unaudited December 31, 2006</u>
Total assets	\$ 57,706,794	\$ 62,083,060
Loans outstanding	18,610,225	19,726,915
Allowance for loan losses	(82,447)	(160,151)
Members' shares	51,471,299	55,374,615
Retained earnings	5,882,447	6,425,010
Net loss for the 11 months ended	(542,563)	

**15. NAME CHANGE**

Effective April 2008, the Credit Union has changed its name to Xceed Financial Credit Union.

**16. RELATED PARTY TRANSACTIONS**

In the normal course of business, the Credit Union extends credit to directors, supervisory committee members and executive officers. The aggregate loans to related parties at December 31, 2007 are approximately \$4,828,705. Deposits from related parties at December 31, 2007 amounted to approximately \$1,828,310.

**17. FAIR VALUE OF FINANCIAL INSTRUMENTS**

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Credit Union's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. The aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Credit Union.

The following methods and assumptions were used by the Credit Union in estimating fair values of financial instruments as disclosed herein:

Cash and Cash Equivalents: The carrying amounts of cash and cash equivalents approximate their fair value.

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Available-for-Sale and Held-to-Maturity Investments: Fair values for investments are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments or on discounted cash flow models which are based on the expected payment characteristics of the underlying mortgage instruments.

Other Investments: The carrying value approximates fair value based on the redemption provisions of the underlying investments.

Loans Receivable: The estimated fair value for all fixed rate loans is determined by discounting the estimated cash flows using the current rate at which similar loans would be made to borrowers with similar credit ratings and maturities.

The estimated fair value for variable rate loans is the carrying amount. The impact of delinquent loans on the estimation of the fair values described above is not considered to have a material effect and, accordingly, delinquent loans have been disregarded in the valuation methodologies employed.

Accrued Interest: Accrued interest receivable represents interest on loans and investments. The carrying amount of accrued interest receivable approximates fair value.

Members' Shares: The fair values disclosed for regular share, share draft and money market accounts are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). Fair values for share certificates are estimated using a discounted cash flow calculation that applies interest rates currently being offered on share certificates to a schedule of aggregated expected monthly maturities on the Credit Union's current share certificates.

Borrowed Funds: The fair values of the Credit Union's borrowed funds are estimated using discounted cash flow analyses based on the Credit Union's incremental borrowing rates for similar types of borrowing arrangements.

State of California Treasury Deposits: The fair values of the Credit Union's State of California treasury deposits are estimated using discounted cash flow analyses based on the Credit Union's incremental deposit rates for similar types of deposit arrangements.

Off-Balance-Sheet Credit-Related Instruments: Fair values for off-balance-sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value for such financial instruments is nominal.

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The estimated fair value of the Credit Union's financial instruments as of December 31, 2007 is summarized as follows:

	<u>Carrying Amount</u>	<u>Fair Value</u>
Financial Assets:		
Cash and cash equivalents	\$ 33,343,000	\$ 33,343,000
Investments available-for-sale	54,733,000	54,733,000
Investments held-to-maturity	1,990,000	1,959,000
Other investments	57,812,000	57,812,000
Loans receivable, net	596,871,000	595,195,000
Accrued interest receivable	2,874,000	2,874,000
Financial Liabilities:		
Members' shares	556,520,000	557,429,000
Borrowed funds	107,300,000	108,630,000
State of California Treasury deposits	10,000,000	10,000,000