

**Digital Federal Credit Union
and Subsidiaries
Consolidated Financial Statements
December 31, 2007 and 2006**

McGladrey & Pullen

Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT

Supervisory Committee
Digital Federal Credit Union and Subsidiaries
Marlborough, Massachusetts

We have audited the accompanying consolidated statements of financial condition of Digital Federal Credit Union (a federally chartered credit union) and Subsidiaries as of December 31, 2007 and 2006 and the related consolidated statements of income, comprehensive income, members' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Credit Union's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits 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 consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Digital Federal Credit Union and Subsidiaries as of December 31, 2007 and 2006 and the consolidated results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

McGladrey & Pullen, LLP

Beverly, Massachusetts

March 27, 2008

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DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

ASSETS		
	2007	2006
Cash and cash equivalents	\$ 227,700	\$ 259,255
Investments		
Available-for-sale	0	2,715
Other	24,580	12,368
Loans held for sale	6,991	8,130
Loans to members, net	3,515,273	3,056,816
Accrued interest receivable	15,547	13,123
Property and equipment, net	62,373	57,308
National Credit Union Share Insurance Fund deposit	26,332	23,021
Other assets	24,955	22,152
	\$ 3,903,751	\$ 3,454,888

LIABILITIES AND MEMBERS' EQUITY

Liabilities		
Members' shares	\$ 3,286,240	\$ 3,191,071
Borrowed funds	325,000	0
Accrued expenses and other liabilities	41,411	35,292
	3,652,651	3,226,363
Total liabilities		
Commitments and contingent liabilities		
Members' Equity		
Retained earnings, substantially restricted	252,211	229,865
Accumulated other comprehensive loss	(1,111)	(1,340)
	251,100	228,525
	\$ 3,903,751	\$ 3,454,888

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

	<u>2007</u>	<u>2006</u>
INTEREST INCOME		
Interest on loans to members	\$ 213,087	\$ 178,720
Interest on investments and cash equivalents	5,784	3,975
	<u>218,871</u>	<u>182,695</u>
INTEREST EXPENSE		
Dividends on members' shares	112,027	87,836
Interest on borrowed funds	4,383	1,476
	<u>116,410</u>	<u>89,312</u>
NET INTEREST INCOME	102,461	93,383
PROVISION FOR LOAN LOSSES	<u>22,250</u>	<u>19,100</u>
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	<u>80,211</u>	<u>74,283</u>
NON-INTEREST INCOME		
Service charges and other fees	16,904	14,908
Interchange income	14,805	13,471
Net gains on sales of loans	1,668	1,184
Loan servicing fees	1,034	1,157
Other non-interest income	1,700	1,972
	<u>36,111</u>	<u>32,692</u>
	<u>116,322</u>	<u>106,975</u>
GENERAL AND ADMINISTRATIVE EXPENSES		
Salaries and benefits	44,689	35,576
Operations	38,598	34,509
Occupancy	10,689	9,195
	<u>93,976</u>	<u>79,280</u>
NET INCOME	<u>\$ 22,346</u>	<u>\$ 27,695</u>

The accompanying notes are an integral part of these statements.

**DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)**

	2007	2006
NET INCOME	\$ 22,346	\$ 27,695
OTHER COMPREHENSIVE INCOME		
Net change in unrealized holding gains on investments classified as available-for-sale	8	127
Minimum pension liability adjustment	221	(38)
Other comprehensive income	229	89
COMPREHENSIVE INCOME	\$ 22,575	\$ 27,784

**DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF MEMBERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)**

	Retained Earnings			Accumulated Other Comprehensive Income (Loss)
	Regular Reserve	Unappropriated	Total	
Balance, December 31, 2005	\$ 42,331	\$ 159,155	\$ 201,486	\$ (1,429)
Net assets acquired in a merger	161	523	684	
Net income		27,695	27,695	
Net change in unrealized gains (losses) on available-for-sale investments				127
Minimum pension liability				(38)
Appropriations	13,250	(13,250)		
Balance, December 31, 2006	55,742	174,123	229,865	(1,340)
Net income		22,346	22,346	
Net change in unrealized gains (losses) on available-for-sale investments				8
Minimum pension liability				221
Appropriations	15,025	(15,025)		
Balance, December 31, 2007	\$ 70,767	\$ 181,444	\$ 252,211	\$ (1,111)

The accompanying notes are an integral part of these statements.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

	<u>2007</u>	<u>2006</u>
OPERATING ACTIVITIES		
Net income	\$ 22,346	\$ 27,695
Adjustments to reconcile net income to net cash provided by operating activities:		
Accretion of investments, net	(4)	(27)
Servicing assets capitalized during the year	(1,091)	(708)
Recovery and expirations in fair value of servicing assets previously written down	0	(484)
Amortization of mortgage servicing rights	649	1,045
Provision for loan losses	22,250	19,100
Depreciation and amortization	4,342	3,793
Net change in:		
Loans held for sale	1,139	3,523
Accrued interest receivable	(2,424)	(2,679)
Other assets	(2,361)	512
Accrued expenses and other liabilities	6,340	1,687
	<u>51,186</u>	<u>53,457</u>
Net cash provided by operating activities		
INVESTING ACTIVITIES		
Proceeds from maturities of available-for-sale investments	2,727	21,133
Net change in other investments	(12,212)	(3,931)
Net change in loans to members	(480,707)	(363,136)
Increase in the National Credit Union Share Insurance Fund deposit	(3,311)	(1,961)
Purchases of property and equipment	(9,407)	(10,290)
Net assets acquired in a merger	0	684
	<u>(502,910)</u>	<u>(357,501)</u>
Net cash used in investing activities		
FINANCING ACTIVITIES		
Net increase (decrease) in borrowed funds	325,000	(100,000)
Net change in members' shares	95,169	435,584
	<u>420,169</u>	<u>335,584</u>
Net cash provided by financing activities		
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(31,555)	31,540
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	259,255	227,715
	<u>\$ 227,700</u>	<u>\$ 259,255</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR		
SUPPLEMENTAL CASH FLOW INFORMATION		
Dividends paid on members' shares and interest paid on notes payable	\$ 117,413	\$ 89,312

**DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006**

1. **SIGNIFICANT ACCOUNTING POLICIES**

Principles of Consolidation: The accompanying consolidated financial statements include the accounts of the Credit Union and its subsidiaries, Financial Vision, LLC, organized for the purpose of software development, DCU Financial Insurance, LLC, which provides financial services to members and DCU Realty, which provides brokerage services to members in Massachusetts. All significant intercompany balances and transactions have been eliminated in consolidation.

Nature of Operations: Digital 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 as defined in the Credit Union's Charter and Bylaws.

Use of Estimates in the Preparation of Financial Statements: The preparation of consolidated 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 consolidated 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: Most of the Credit Union's business activity is with its members who reside in or are employed in the Northeastern part of the United States of America. 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 the Northeastern part of the United States of America. However, the loan portfolio is well diversified and the Credit Union does not have any significant concentrations of credit risk except unsecured loans, which by their nature increase the risk of loss compared to those loans that are collateralized. The Credit Union's policy for repossessing collateral is that when all other collection efforts have been exhausted, the Credit Union enforces its first lien holder status and repossesses the collateral. The Credit Union has full and complete access to repossessed collateral. Repossessed collateral normally consists of vehicles and residential real estate.

Cash and Cash Equivalents: For the purpose of the consolidated statements of financial position and the consolidated statements 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 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 (loss).

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

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 .35% of the Credit Union's Membership Stock Investment Base. In addition to the Membership Stock Investment Base, the Credit Union is required to maintain an investment in capital stock of the FHLB in an amount equal to 4.0% of advances from the FHLB. No ready market exists for the FHLB stock, and it has no quoted market value.

Loans Held for Sale: Mortgage loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or estimated market value. All sales are made without recourse.

Loans to Members: The Credit Union grants mortgage, commercial and consumer loans to members. 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 90 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 non-accrual 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 non-accrual 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 fee or 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.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

Allowance for Loan Losses: The allowance for loan losses is established as losses are estimated to have occurred through 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 loss 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 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.

Other Real Estate Owned: Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Other real estate owned are reported in other assets and revenue and expenses from operations and changes in the valuation allowance are included in other non-interest income.

Property and Equipment: Land is carried at cost. Land improvements, building and improvements, and furniture and equipment and leasehold improvements are carried at cost, less accumulated depreciation and amortization. Building and improvements 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. Construction in progress is carried at cost and will be depreciated using the straight-line method over the estimated useful life of the asset once placed in service.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

Loan Servicing: Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. Capitalized servicing rights are reported in other assets and are amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. If the Credit Union later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income.

Servicing fee income is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal; or a fixed amount per loan and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income.

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 and 2006 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.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

Advertising Costs: Advertising costs are expensed as incurred.

Income Taxes: The Credit Union is exempt, by statute, from federal and state income taxes. Since the Credit Union's subsidiaries are organized as Limited Liability Companies, they effectively pay no taxes.

Pension Plan: The Credit Union has a qualified, noncontributory defined-benefit pension plan covering substantially all of its employees. The Credit Union's policy is to fund the minimum amount required under ERISA.

Comprehensive Income (Loss): 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 consolidated statements of financial condition. For 2007 and 2006, other comprehensive income (loss) includes no reclassification adjustments.

Reclassifications: Certain account reclassifications have been made to the 2006 consolidated financial statements in order to conform to classifications used in the current year.

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. This Statement is effective for fiscal years beginning after November 15, 2007. 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 consolidated 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 consolidated 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, if any, on its consolidated financial position, results of operations and cash flows.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

2. INVESTMENTS

Investments classified as available-for-sale consist of the following (in thousands):

<u>December 31, 2006</u>	<u>Amortized Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Mortgage-backed securities	\$ 2,723	\$ 0	\$ (8)	\$ 2,715

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 2006 are as follows (in thousands):

<u>December 31, 2006</u>	<u>Fair Value</u>	<u>Continuous Unrealized Losses Existing For:</u>		<u>Total Unrealized Losses</u>
		<u>Less Than 12 Months</u>	<u>More Than 12 Months</u>	
Available-for-sale				
Mortgage-backed securities	\$ 2,715	\$ 0	\$ (8)	\$ (8)

At December 31, 2006, the investment portfolio included 2 securities 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.

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 (in thousands):

	<u>December 31</u>	
	<u>2007</u>	<u>2006</u>
FHLB stock	\$ 18,715	\$ 6,503
Paid-in-capital account in a corporate credit union	5,000	5,000
Other	865	865
	<u>\$ 24,580</u>	<u>\$ 12,368</u>

The paid-in-capital account is an uninsured equity capital accounts and is redeemable only if called by the corporate credit union. The fair value of other investments approximates book value.

FHLB stock, paid-in-capital and other investment accounts have no contractual maturity.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

3. LOANS TO MEMBERS

Loans to members consist of the following (in thousands):

	December 31	
	2007	2006
Mortgage loans:		
Fixed rate	\$ 415,928	\$ 321,390
Home equity, fixed and variable rate	355,162	328,075
Variable rate	5,784	5,641
Hybrid	881,160	749,002
Home equity line of credit, variable rate	424,816	409,080
Construction commercial	32,628	27,237
Commercial real estate	223,236	174,059
	2,338,714	2,014,484
Vehicle loans	749,019	673,494
Commercial loans	44,846	32,557
Credit card loans, unsecured	300,504	261,381
Other consumer loans	86,271	74,648
	3,519,354	3,056,564
Deferred net loan origination costs	17,280	16,962
Allowance for loan losses	(21,361)	(16,710)
	\$ 3,515,273	\$ 3,056,816

The Credit Union offers non-traditional mortgage loans to its members. These loans include hybrid loans which consist of loans that are fixed for an initial period of three, five, seven or ten years. After this period, the mortgages are converted to variable rate using the fully indexed rate, which can result in significant payment shock to the borrower.

Non-traditional mortgage loans may have significantly different credit risk characteristics than traditional fixed and variable rate mortgages. However, the Credit Union believes it has established prudent underwriting standards as well as adequate risk management functions to monitor these additional risks.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

The following is an analysis of the allowance for loan losses (in thousands):

	Years Ended December 31	
	2007	2006
Balance, beginning of year	\$ 16,710	\$ 14,651
Provision for loan losses	22,250	19,100
Recoveries	1,125	1,373
Loans charged off	(18,724)	(18,481)
Allowance for loan losses acquired in merger	0	67
Balance, end of year	<u>\$ 21,361</u>	<u>\$ 16,710</u>

Loans on which accrual of interest has been discontinued or reduced amounted to \$20,799,000 and \$13,488,000, respectively, at December 31, 2007 and 2006.

4. LOAN SERVICING

Mortgage loans serviced for others are not included in the accompanying consolidated statements of financial condition. The unpaid principal balances of these loans amounted to \$697,671,000 and \$664,988,000, respectively, at December 31, 2007 and 2006.

A summary of the changes in the balance of mortgage servicing rights in 2007 and 2006 were as follows (in thousands):

	Years Ended December 31	
	2007	2006
Balance, beginning of year	\$ 5,476	\$ 5,329
Servicing assets capitalized during the year	1,091	708
Recovery and expirations in fair value of servicing assets previously written down	0	484
Amortization of servicing assets	(649)	(1,045)
Balance, end of year	<u>\$ 5,918</u>	<u>\$ 5,476</u>
Fair value of mortgage servicing rights	\$ 5,918	\$ 5,944

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006

The aggregate changes in the valuation allowances for mortgage servicing rights in 2007 and 2006 were as follows (in thousands):

	Years Ended December 31	
	2007	2006
Balance, beginning of year	\$ 355	\$ 839
Recovery and expirations in fair value of servicing assets previously written down	0	(484)
Balance, end of year	\$ 355	\$ 355

The key economic assumptions used in determining the fair value of mortgage servicing rights at December 31, 2007 and 2006 are as follows:

	December 31	
	2007	2006
Prepayment speed	12.00-12.70%	10.20% - 10.40%
Yield to maturity discount rate	5.00%	5.00%

5. PROPERTY AND EQUIPMENT

Property and equipment are summarized as follows (in thousands):

	December 31	
	2007	2006
Land and improvements	\$ 9,736	\$ 9,732
Building and improvements	47,734	45,713
Furniture and equipment and leasehold improvements	29,127	21,260
Construction in progress	762	2,457
	87,359	79,162
Accumulated depreciation and amortization	(24,986)	(21,854)
	\$ 62,373	\$ 57,308

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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The Credit Union leases various 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 (in thousands):

<u>Years Ending December 31</u>	
2008	\$ 1,918
2009	1,661
2010	1,485
2011	1,511
2012	1,292
Subsequent years	4,482
	<hr/>
	\$ 12,349
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Rental expense for the years ended December 31, 2007 and 2006 for all facilities leased under operating leases totaled \$2,249,000 and \$1,980,000, respectively.

6. MEMBERS' SHARES

Members' shares are summarized as follows (in thousands):

	<u>December 31</u>	
	<u>2007</u>	<u>2006</u>
Regular shares	\$ 669,961	\$ 597,787
Share draft accounts	531,113	499,172
Money market accounts	414,490	392,464
Individual retirement accounts	19,037	18,193
Certificates	1,651,639	1,683,455
	<hr/>	<hr/>
	\$ 3,286,240	\$ 3,191,071
	<hr/>	<hr/>

Shares by maturity as of December 31, 2007 are summarized as follows (in thousands):

No contractual maturity	\$ 1,634,601
0 – 1 year maturity	1,415,816
1 – 2 years maturity	116,308
2 – 3 years maturity	53,098
3 – 4 years maturity	22,909
4 – 5 years maturity	43,505
Over 5 years maturity	3
	<hr/>
	\$ 3,286,240
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DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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Regular shares, share draft accounts, money market accounts, and individual retirement account shares have no contractual maturity. Certificate accounts have maturities of six 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 and 2006 is approximately \$458,456,000 and \$841,287,000, respectively.

7. BORROWED FUNDS

The Credit Union utilizes a demand loan agreement with the Federal Home Loan Bank (FHLB) of Boston. The terms of the agreement call for pledging a portion of the Credit Union's mortgage portfolio. The agreement provides for a maximum borrowing amount determined on a continual basis by the Credit Union and the FHLB. At December 31, 2007 and 2006, respectively, there were advances of \$325,000,000 and \$0 outstanding with interest rates ranging from 3.99% to 5.16% and maturity dates ranging from June 5, 2008 to December 28, 2009.

The Credit Union utilizes a demand loan agreement with a corporate credit union. The terms of this agreement call for the pledging of certain assets as security for any and all obligations taken by the Credit Union under this agreement. The agreement provides for a credit limit of \$350,000,000 with interest charged at a rate determined by the lender on a periodic basis. At December 31, 2007 and 2006, there were no borrowings under this agreement. The agreement is reviewed for continuation by the lender and the Credit Union annually.

The Credit Union also has access to an Ideal Way line of credit with the FHLB. The agreement provides for a credit limit of \$1,000,000, with interest charged at a rate determined by the lender on a periodic basis. At December 31, 2007 and 2006, there were no borrowings under this agreement.

8. 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 consolidated financial statements.

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 consolidated financial statements.

Outstanding mortgage loan commitments at December 31, 2007 total approximately \$26,978,000.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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Unfunded loan commitments under lines of credit are summarized as follows (in thousands):

	December 31	
	2007	2006
Home equity	\$ 657,383	\$ 681,324
Credit card	1,163,609	1,124,975
Commercial	46,962	20,745
Other consumer	25,593	24,507
	\$ 1,893,547	\$ 1,851,551

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.

Unfunded commitments under commercial lines-of-credit, revolving credit lines and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines-of-credit are uncollateralized and usually do not contain a specified maturity date and ultimately may not be drawn upon to the total extent to which the Credit Union is committed.

9. ON-BALANCE SHEET DERIVATIVE INSTRUMENTS

Certain derivative instruments do not meet SFAS No. 133 hedging requirements. These undesignated derivative instruments are recognized on the consolidated statements of financial condition at fair value, with changes in fair value recorded in operations expenses.

Derivative Loan Commitments: Mortgage loan commitments are referred to as derivative loan commitments if the loan that will result from exercise of the commitment will be held for sale upon funding. The Credit Union enters into commitments to fund residential mortgage loans at specified times in the future, with the intention that these loans will subsequently be sold in the secondary market. A mortgage loan commitment binds the Credit Union to lend funds to a potential borrower at a specified interest rate and within a specified period of time, generally up to 60 days after inception of the rate lock.

Outstanding derivative loan commitments expose the Credit Union to the risk that the price of the loans arising from exercise of the loan commitment might decline from inception of the rate lock to funding of the loan due to increases in mortgage interest rates. If interest rates increase, the value of these loan commitments decreases. Conversely, if interest rates decrease, the value of these loan commitments increases. The notional amount of undesignated mortgage loan commitments was \$3,012,000 and \$3,183,000 at December 31, 2007 and 2006, respectively.

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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Forward Loan Sale Commitments: To protect against the price risk inherent in derivative loan commitments, the Credit Union utilizes both “mandatory delivery” and “best efforts” forward loan sale commitments to mitigate the risk of potential decreases in the values of loans that would result from the exercise of the derivative loan commitments.

With a “mandatory delivery” contract, the Credit Union commits to deliver a certain principal amount of mortgage loans to an investor at a specified price on or before a specified date. If the Credit Union fails to deliver the amount of mortgages necessary to fulfill the commitment by the specified date, it is obligated to pay a “pair-off” fee, based on then-current market prices, to the investor to compensate the investor for the shortfall.

With a “best efforts” contract, the Credit Union commits to deliver an individual mortgage loan of a specified principal amount and quality to an investor if the loan to the underlying borrower closes. Generally, the price the investor will pay the seller for an individual loan is specified prior to the loan being funded (for example, on the same day the lender commits to lend funds to a potential borrower).

The Credit Union expects that these forward loan sale commitments will experience changes in fair value opposite to the change in fair value of derivative loan commitments. The notional amount of undesignated forward loan sale commitments was \$4,658,000 and \$5,175,000 at December 31, 2007 and 2006, respectively.

10. 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.

The Credit Union has no outstanding commitments to sell loans or investments at December 31, 2007.

11. EMPLOYEE BENEFITS

The Credit Union sponsors a defined benefit pension plan for the benefit of its employees based on years of service. The plan calls for benefits to be paid to eligible employees at retirement equal to (a) 1.5% of their average five year compensation up to the integration level (as defined) plus (b) a 0.5% of their average five year compensation in excess of the integration level c) multiplied by years of service. The maximum number of years of service credited is 20 years. Effective January 31, 2002, the Plan was frozen. Accordingly, the participants ceased to earn additional benefits under the Plan, and no additional employees shall become eligible to participate in the Plan.

**DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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Adoption of FASB Statement No. 158

The Credit Union adopted the recognition and disclosure provisions of SFAS 158 on December 31, 2007. SFAS 158 required the Credit Union to recognize the funding status of its defined benefit pension plan in the December 31, 2007 consolidated statement of financial condition, with a corresponding adjustment to accumulated other comprehensive income (loss). The adjustment to accumulated other comprehensive income (loss) at adoption represents the net unrecognized actuarial losses and unrecognized prior service costs remaining from the initial adoption of SFAS No. 87, "Employers' Accounting for Pensions" ("SFAS 87"), all of which were previously netted against that plan's funded status in the Credit Union's consolidated statement of financial condition pursuant to the provisions of SFAS 87. These amounts will be subsequently recognized as net periodic pension plan cost pursuant to the Credit Union's historical accounting policy for amortizing such amounts. Further, actuarial gains and losses that arise in subsequent periods and are not recognized as net periodic pension cost in the same period will be recognized as a component of other comprehensive income (loss). Those amounts will be subsequently recognized as a component of net periodic pension plan cost on the same basis as the amounts recognized in accumulated other comprehensive income (loss) at adoption of SFAS 158.

The incremental effects of adopting the provisions of Statement 158 on the Credit Union's statement of financial condition at December 31, 2007 are presented in the following table (in thousands):

	At December 31, 2007 Debit (Credit)		
	Prior to Adopting Statement of 158	Effect of Adopting Statement of 158	As reported at December 31, 2007
Prepaid pension costs	\$ 0	\$ 76	\$ 76
Liability for pensions	\$ (145)	\$ 145	\$ 0
Accumulated other comprehensive income (loss)	\$ 1,332	\$ (221)	\$ 1,111
		September 30	
		2007	2006
Benefit obligation at September 30		\$ 5,434	\$ 5,359
Fair value of plan assets		5,461	4,783
Funded status		\$ 27	\$ (576)
Accumulated benefit obligation		\$ 5,434	\$ 5,359

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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	September 30	
	2007	2006
Assumptions used to determine benefit obligation:		
Discount rate	6.00%	6.00%
Rate of compensation increase	N/A	N/A

	Years Ended	
	2007	2006
Net pension cost	\$ (28)	\$ (19)
Employer contribution	\$ 402	\$ 187
Plan participants' contributions	\$ 0	\$ 0
Benefit payments	\$ (299)	\$ (214)

	September 30	
	2007	2006
Assumptions used to determine net pension cost:		
Discount rate	6.00%	6.00%
Expected long-term return on plan assets	8.00%	8.00%
Rate of compensation increase	N/A	N/A

The 8.00% expected long-term return on plan assets assumption was derived from historical rates of return of stocks, government bonds and 30 day T-bills, assuming a portfolio comprised of 55% equity securities, 45% bonds and 5% cash and cash equivalents.

Amounts recognized in the consolidated statement of financial condition as of December 31, 2007 consist of (in thousands):

Noncurrent assets	\$	27
Employer Contributions after measure date		49
Current liabilities		0
Noncurrent liabilities		0
		0
Net amount recognized	\$	76

DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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Amounts recognized in accumulated other comprehensive loss as of December 31, 2007 consist of (in thousands):

Loss/(gain)	\$ 1,111
Prior service cost (credit)	0
Transition asset/obligation	0
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	\$ 1,111
	<hr/>

The following are the amounts in accumulated other comprehensive income (loss) expected to be recognized as components of net periodic pension cost over the next fiscal year ending December 31, 2008 (in thousands).

Gain/loss	\$ 29
Prior service cost	\$ 0
Transition asset/obligation	\$ 0

The Credit Union's pension plan weighted-average asset allocations by asset category are as follows:

	September 30	
	2007	2006
Equity securities	41%	42%
Bonds	15%	14%
Cash and cash equivalents	44%	44%
	<hr/>	<hr/>
	100%	100%
	<hr/>	<hr/>

The plan's investment policies and strategies are diversified to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to so. The plan may employ one or more investment managers of varying styles and philosophies to attain the account's objectives.

The Credit Union expects to contribute \$218,000 to the plan in 2008.

The following pension benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows (in thousands):

<u>Years Ending December 31</u>	
2008	\$ 97
2009	109
2010	147
2011	182
2012	208
2013 – 2017	1,458
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	\$ 2,201
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DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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The Credit Union has a defined contribution 401(k) plan that allows employees to defer a portion of their salary into the plan. The Credit Union has the option of making a matching and/or a profit sharing contribution. The total 401(k) plan expense for the years ended December 31, 2007 and 2006 was \$1,468,000 and \$1,194,000, respectively. Plan costs are accrued and funded on a current basis.

The Credit Union has incentive bonuses and 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 for a specified period of time. If these employees become fully disabled as defined in certain agreements, accrued benefits are immediately payable. The benefits are subject to forfeiture if employment is terminated for cause as defined in the agreements. The estimated liability under the agreements is being accrued as defined in the plans over the remaining years.

12. 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 consolidated 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 accounting principles generally accepted in the United States of America. 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 requirements as of December 31, 2007 and 2006 were 5.27% and 5.28%, respectively. The minimum requirement to be considered "complex" under the regulatory framework is 6%. Management believes, as of December 31, 2007 and 2006, that the Credit Union meets all capital adequacy requirements to which it is subject.

As of December 31, 2007 and the most recent call reporting period, the NCUA categorized the Credit Union as adequately capitalized under the regulatory framework for prompt corrective action and, therefore, net worth and the regular reserve account must increase quarterly by .1% of assets.

As of December 31, 2006, 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.

**DIGITAL FEDERAL CREDIT UNION AND SUBSIDIARIES
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The Credit Union's actual capital amounts and ratios are presented in the following table (in thousands):

	<u>December 31, 2007</u>		<u>December 31, 2006</u>	
	<u>Amount</u>	<u>Ratio/Requirement</u>	<u>Amount</u>	<u>Ratio/Requirement</u>
➤ Amount needed to be classified as "adequately capitalized"	\$ 234,225	6.00%	\$ 196,736	6.00%
➤ Amount needed to be classified as "well capitalized"	\$ 273,263	7.00%	\$ 229,525	7.00%
➤ Actual net worth	\$ 252,211	6.81%	\$ 229,865	7.01%

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 average of the quarter-end balances of the four most recent quarters option, as permitted by regulation.

13. BUSINESS COMBINATION

On September 30, 2006, the Credit Union merged with Charles River Credit Union. The merger was accounted for similar to a pooling of interest. The statement of financial condition and the results of operations and cash flows of Charles River Credit Union prior to the merger date were not included in the consolidated financial statements, since the effect would have not been significant.

14. 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 and 2006 are approximately \$1,912,000 and \$1,576,000, respectively. Deposits from related parties at December 31, 2007 and 2006 amounted to approximately \$1,249,000 and \$1,108,000, respectively.

15. 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 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.

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

Loans to Members: For variable-rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values. Fair values for certain mortgage loans (for example, one-to-four family residential), credit-card loans, and other consumer loans are based on quoted market prices of similar loans sold in conjunction with securitization transactions, adjusted for differences in loan characteristics. Fair values for business real estate and business loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

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 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). The carrying amounts of variable-rate, fixed-term share certificates approximate their fair values at the reporting date. Fair values for fixed-rate shares and share certificates are estimated using a discounted cash flow calculation that applies interest rates currently being offered on shares and certificates to a schedule of aggregated expected monthly maturities on shares and 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.

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 is summarized as follows (in thousands):

	December 31, 2007		December 31, 2006	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial Assets:				
Cash and cash equivalents	\$ 227,700	\$ 227,700	\$ 259,255	\$ 259,255
Investments available-for-sale	0	0	2,715	2,715
Other investments	24,580	24,580	12,368	12,368
Loans held for sale	6,991	6,991	8,130	8,130
Loans to members, net	3,515,273	3,493,807	3,056,816	3,028,629
Accrued interest receivable	15,547	15,547	13,123	13,123
Financial Liabilities:				
Members' shares	3,286,240	3,292,422	3,191,071	3,188,992
Borrowed funds	325,000	347,760	0	0