

FLAGSTAR BANCORP INC
Form 10-Q
August 07, 2017
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

OR

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

For the transition period from _____ to _____

Commission File Number: 001-16577

(Exact name of registrant as specified in its charter).

Michigan 38-3150651
(State or other jurisdiction of (I.R.S. Employer
Incorporation or organization) Identification No.)

5151 Corporate Drive, Troy, Michigan 48098-2639
(Address of principal executive offices) (Zip code)
(248) 312-2000
(Registrant's telephone number, including area code)

Not applicable
(Former name, former address and formal fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act .

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

As of August 3, 2017, 57,161,639 shares of the registrant's common stock, \$0.01 par value, were issued and outstanding.

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GLOSSARY OF ABBREVIATIONS AND ACRONYMS

The following list of abbreviations and acronyms are provided as a tool for the reader and may be used throughout this Report, including the Consolidated Financial Statements and Notes:

Term	Definition	Term	Definition
AFS	Available for Sale	GAAP	United States Generally Accepted Accounting Principles
Agencies	Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, and Government National Mortgage Association, Collectively	HELOC	Home Equity Lines of Credit
ALCO	Asset Liability Committee	HELOAN	Home Equity Loan
ALLL	Allowance for Loan & Lease Losses	Home equity	second mortgages, HELOANs, HELOCs
AOCI	Accumulated Other Comprehensive Income (Loss)	HTM	Held to Maturity
ASU	Accounting Standards Update	LIBOR	London Interbank Offered Rate
Basel III	Basel Committee on Banking Supervision Third Basel Accord	LHFI	Loans Held-for-Investment
C&I	Commercial and Industrial	LHFS	Loans Held-for-Sale
CDARS	Certificates of Deposit Account Registry Service	LTV	Loan-to-Value
CFPB	Consumer Financial Protection Bureau	Management	Flagstar Bancorp's Management
CLTV	Combined Loan to Value	MBIA	MBIA Insurance Corporation
Common Stock	Common Shares	MBS	Mortgage-Backed Securities
CRE	Commercial Real Estate	MD&A	Management's Discussion and Analysis
DFAST	Dodd-Frank Stress Test	MSR	Mortgage Servicing Rights
DOJ	United States Department of Justice	N/A	Not Applicable
DTA	Deferred Tax Asset	NYSE	New York Stock Exchange
EVE	Economic Value of Equity	OCC	Office of the Comptroller of the Currency
Fannie Mae/FNMA	Federal National Mortgage Association	OTTI	Other-Than-Temporary-Impairment
FASB	Financial Accounting Standards Board	QTL	Qualified Thrift Lending
FDIC	Federal Deposit Insurance Corporation	RWA	Risk Weighted Assets
FHA	Federal Housing Administration	SEC	Securities and Exchange Commission
FHLB	Federal Home Loan Bank	TARP Preferred	Troubled Asset Relief Program Fixed Rate Cumulative Perpetual Preferred Stock, Series C
FICO	Fair Isaac Corporation	TDR	Trouble Debt Restructuring
FRB	Federal Reserve Bank	UPB	Unpaid Principal Balance
Freddie Mac	Federal Home Loan Mortgage Corporation	U.S. Treasury	United States Department of Treasury
FTE	Full Time Equivalent	VIE	Variable Interest Entities
		XBRL	eXtensible Business Reporting Language

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PART I. FINANCIAL INFORMATION

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following is Management's Discussion and Analysis of the financial condition and results of operations of Flagstar Bancorp, Inc. for the second quarter of 2017, which should be read in conjunction with the financial statements and related notes set forth in Item 1 of this Form 10-Q and Flagstar Bancorp, Inc.'s 2016 Annual Report on Form 10-K for the year ended December 31, 2016.

Certain statements in this Form 10-Q, including but not limited to statements included within the Management's Discussion and Analysis of Financial Condition and Results of Operations, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. These statements are based on the current beliefs and expectations of our management. Actual results may differ from those set forth in forward-looking statements. See Forward-Looking Statements on page 38 of this Form 10-Q and Part I, Item 1A, Risk Factors of Flagstar Bancorp, Inc.'s 2016 Annual Report or Form 10-K for the year ended December 31, 2016. Additional information about Flagstar can be found on our website at www.flagstar.com.

Where we say "we," "us," "our," the "Company," "Bancorp" or "Flagstar," we usually mean Flagstar Bancorp, Inc. However, in some cases, a reference to "we," "us," "our," the "Company" or "Flagstar" will include our wholly-owned subsidiary Flagstar Bank, FSB (the "Bank"). See the Glossary of Abbreviations and Acronyms on page 3 for definitions used throughout this Form 10-Q.

Introduction

We are a Michigan-based savings and loan holding company founded in 1993. Our business is primarily conducted through our principal subsidiary, the Bank, a federally chartered stock savings bank founded in 1987. Based on our assets at June 30, 2017, we are one of the largest banks headquartered in Michigan, providing commercial, small business, and consumer banking services. At June 30, 2017, we had 3,432 full-time equivalent employees inclusive of account executives and loan officers. Our common stock is listed on the NYSE under the symbol "FBC." We are considered a controlled company for NYSE purposes, because MP Thrift Investments, L.P. held approximately 62.3 percent of our common stock as of June 30, 2017.

Our banking network emphasizes the delivery of a complete set of banking and mortgage products and services and we distinguish ourselves by crafting specialized solutions for our customers, local delivery, customer service and competitive product pricing. At June 30, 2017, we operated 99 full service banking branches throughout Michigan's major markets where we offer a full set of banking products to consumer, commercial, and government customers.

We have a unique, relationship-based business model of a leading Michigan-based bank leveraging a national mortgage business. We believe our strong position and focus on service creates a significant competitive advantage in the markets in which we compete. The disciplined management team we have assembled is focused on developing substantial and attractive growth opportunities that generate profitable results from operations. We believe our lower risk profile and strong capital level position us to better exploit the opportunities that our business model yields and deliver attractive shareholder returns over the long term.

Nationally, we are the 5th largest bank mortgage originator and we utilize multiple origination channels including correspondent, broker, distributed retail, and direct to consumer. We also service and subservice mortgage loans for others on a fee for service basis and may also collect ancillary fees, such as late fees and earn income through the use of noninterest-bearing escrow deposits. These escrow deposit accounts and amounts received from servicing loans generate company controlled deposits which offer a stable, low cost, long-term source of funding.

Operating Segments

Our operations are conducted through three operating segments: Community Banking, Mortgage Originations, and Mortgage Servicing. Additionally, our Other segment includes the remaining reported activities. For additional information, please see MD&A - Operating Segments and Note 18 - Segment Information.

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Selected Financial Ratios

(Dollars in millions, except share data)

	Three Months Ended		Six Months Ended		
	June 30, 2017	2016 (1)	June 30, 2017	2016 (1)	
Selected Ratios:					
Interest rate spread	2.59	% 2.43	% 2.55	% 2.46	%
Net interest margin	2.77	% 2.63	% 2.72	% 2.64	%
Return on average assets	1.04	% 1.38	% 0.91	% 1.27	%
Return on average equity	11.57	% 11.53	% 9.77	% 10.81	%
Return on average common equity	11.57	% 13.83	% 9.77	% 13.00	%
Equity/assets ratio (average for the period)	9.02	% 11.95	% 9.29	% 11.73	%
Efficiency ratio	72.0	% 68.2	% 74.2	% 71.2	%
Average Balances:					
Average common shares outstanding	57,101,816	56,574,796	57,012,208	56,544,256	
Average fully diluted shares outstanding	58,138,938	57,751,230	58,106,070	57,623,081	
Average interest-earning assets	\$ 14,020	\$ 11,639	\$ 13,187	\$ 11,755	
Average interest paying liabilities	\$ 11,804	\$ 9,205	\$ 11,066	\$ 9,514	
Average stockholders' equity	\$ 1,418	\$ 1,606	\$ 1,382	\$ 1,583	
		June 30, 2017	December 31, 2016	June 30, 2016 (1)	
Selected Statistics:					
Book value per common share		\$ 24.64	\$ 23.50	\$ 23.54	
Tangible book value per share (2)		\$ 24.29	\$ 23.50	\$ 23.54	
Number of common shares outstanding		57,161,431	56,824,802	56,575,779	
Equity-to-assets ratio		8.82	% 9.50	% 11.65	%
Common equity-to-assets ratio		8.82	% 9.50	% 9.70	%
Capitalized value of MSRs		1.14	% 1.07	% 0.99	%
Bancorp Tier 1 leverage (to adjusted avg. total assets) (3)		9.10	% 8.88	% 11.59	%
Bank Tier 1 leverage (to adjusted avg. total assets)		10.26	% 10.52	% 12.03	%
Mortgage rate lock commitments (fallout-adjusted) (4)		\$ 9,002	\$ 6,091	\$ 8,127	
Mortgage loans sold and securitized		\$ 8,989	\$ 8,422	\$ 14,888	
Number of banking centers		99	99	99	
Number of FTE		3,432	2,886	2,894	

(1) Includes TARP Preferred which was redeemed in the third quarter 2016.

Excludes goodwill and intangibles of \$20 million, zero, and zero at June 30, 2017, December 31, 2016, and June 30, 2016, respectively, included in Other Assets on the Consolidated Statement of Financial Condition. See Non-GAAP Financial Measures for further information.

(3) Basel III transitional.

(4) Fallout adjusted refers to mortgage rate lock commitments which are adjusted by a percentage of mortgage loans in the pipeline that are not expected to close based on previous historical experience and the level of interest rates.

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Executive Overview

The second quarter 2017 resulted in solid earnings of \$41 million, or \$0.71 per diluted share. Our community bank results continued to be outstanding. Average warehouse loans increased from the first quarter, growing 23 percent, and we saw a 15 percent increase in average commercial and industrial and commercial real estate loans. We also posted a 10 basis point increase in net interest margin, maintaining a stable deposit cost despite recent Federal Reserve rate increases. The maturation of our community bank has generated a more balanced, more sustainable earnings stream for our Company.

Our mortgage origination segment also had an outstanding quarter. In the first half of 2017, fallout-adjusted locks rose 48 percent to \$9.0 billion, driven primarily by the impact of the acquisitions of Opes Advisors (Opes) this quarter, as well as the delegated correspondent business from Stearns Lending (Stearns) last quarter. With the addition of Opes, we have more than tripled our distributed retail origination volume and believe we are now in a strong position for the move to a purchase mortgage market.

In second quarter 2017, we closed on the previously reported bulk sales of \$191 million of MSR, successfully executing our MSR reduction strategy and releasing capital to support balance sheet growth. We are the servicer on approximately 85 percent of the MSR we sold, providing a boost to our servicing business and helping us to exceed over 400,000 accounts serviced or subserviced. Our MSR now stand at 15 percent of our tier 1 common equity, positioning us well for the full phase-in of Basel III.

We have a formidable banking business, an industry-leading mortgage origination platform and a blossoming servicing business, all of which are supported by strong capital and liquidity. Nationally, we are the 5th largest bank mortgage originator and a top 10 servicer. This combination positions us to grow our balance sheet with higher quality, relationship-focused assets and continues to create value for our shareholders.

Earnings Performance

	Three Months Ended June 30, 2017			Six Months Ended June 30, 2017		
	2016	Change	2016	2016	Change	
	(Dollars in millions, except share data)					
Net interest income	\$97	\$20	\$77	\$180	\$24	
Provision (benefit) for loan losses	(1)	2	(3)	(16)	18	
Total noninterest income	116	(12)	128	216	(17)	
Total noninterest expense	154	15	139	294	18	
Provision for income taxes	19	(3)	22	32	(11)	
Net income	\$41	\$(6)	\$47	\$68	\$(18)	
Income per share						
Basic	\$0.72	\$0.05	\$0.67	\$1.18	\$(0.05)	
Diluted	\$0.71	\$0.05	\$0.66	\$1.16	\$(0.05)	

Net income decreased \$6 million for the three months ended June 30, 2017, compared to the three months ended June 30, 2016. Net interest income increased \$20 million for the three months ended June 30, 2017, compared to the three months ended June 30, 2016. This increase was primarily driven by a \$2.4 billion increase in interest-earning assets led by strong commercial loan growth and an increase in LHFS. The improvement in net interest income was more than offset by a \$12 million decrease in noninterest income resulting from a decrease in net gain on loan sales and a \$15 million increase in noninterest expense due to increases in compensation and benefits from increased headcount due to recent acquisitions. Diluted income per share increased to \$0.71 for the three months ended June 30,

2017, compared to \$0.66 for the three months ended June 30, 2016, partially due to the payoff of our TARP Preferred which occurred in the third quarter of 2016.

Net income decreased \$18 million for the six months ended June 30, 2017, compared to the six months ended June 30, 2016. Net interest income increased \$24 million for the six months ended June 30, 2017, compared to the six months ended June 30, 2016, primarily driven by growth in interest-earning assets. This was more than offset by a decrease in noninterest income of \$17 million, primarily due to lower net gain on loan sales and an increase in noninterest expense of \$18 million, primarily driven by higher compensation and benefits driven by increased headcount resulting from acquisitions, as well as an increase in the provision for loan losses. In the six months ended June 30, 2017, our provision of \$2 million reflects the strong credit quality of our loan portfolios and a low level of net losses. The \$16 million benefit for the six months ended June 30, 2016 resulted primarily from the sale of \$1.2 billion UPB of performing and \$110 million UPB of nonperforming loans.

Net Interest Income

The following tables present, on a consolidated basis, interest income from average assets and liabilities, expressed in dollars and yields:

	Three Months Ended June 30,							
	2017				2016			
	Average Balance	Interest	Yield/ Rate	%	Average Balance	Interest	Yield/ Rate	%
	(Dollars in millions)							
Interest-Earning Assets								
Loans held-for-sale	\$4,269	\$ 42	4.00	%	\$2,884	\$ 26	3.64	%
Loans held-for-investment								
Residential first mortgage	2,495	21	3.38	%	2,232	18	3.15	%
Home equity	439	6	4.91	%	485	6	4.91	%
Other	27	—	4.54	%	29	—	4.92	%
Total Consumer loans	2,961	27	3.61	%	2,746	24	3.48	%
Commercial Real Estate	1,477	16	4.16	%	899	8	3.41	%
Commercial and Industrial	936	11	4.77	%	607	6	3.97	%
Warehouse Lending	850	10	4.71	%	1,317	14	4.28	%
Total Commercial loans	3,263	37	4.48	%	2,823	28	3.94	%
Total loans held-for-investment (1)	6,224	64	4.07	%	5,569	52	3.71	%
Loans with government guarantees	295	3	4.02	%	444	4	3.33	%
Investment securities	3,166	20	2.57	%	2,558	17	2.66	%
Interest-earning deposits	66	—	1.07	%	184	—	0.50	%
Total interest-earning assets	14,020	129	3.69	%	11,639	99	3.40	%
Other assets	1,690				1,799			
Total assets	\$15,710				\$13,438			
Interest-Bearing Liabilities								
Retail deposits								
Demand deposits	\$510	\$ —	0.15	%	\$482	\$ —	0.17	%
Savings deposits	3,933	8	0.75	%	3,691	7	0.79	%
Money market deposits	239	—	0.42	%	363	1	0.52	%
Certificates of deposit	1,094	3	1.08	%	951	2	1.00	%
Total retail deposits	5,776	11	0.75	%	5,487	10	0.75	%
Government deposits								
Demand deposits	200	—	0.39	%	203	—	0.39	%
Savings deposits	411	1	0.56	%	398	—	0.52	%
Certificates of deposit	291	—	0.68	%	410	1	0.50	%
Total government deposits	902	1	0.56	%	1,011	1	0.49	%
Wholesale deposits and other	4	—	0.48	%	—	—	—%	
Total interest-bearing deposits	6,682	12	0.72	%	6,498	11	0.71	%
Short-term Federal Home Loan Bank advances and other	3,429	8	0.98	%	835	1	0.41	%
Long-term Federal Home Loan Bank advances	1,200	6	1.91	%	1,625	8	1.93	%
Other long-term debt	493	6	5.06	%	247	2	3.31	%
Total interest-bearing liabilities	11,804	32	1.10	%	9,205	22	0.97	%
Noninterest-bearing deposits (2)	2,057				2,133			
Other liabilities	431				494			
Stockholders' equity	1,418				1,606			
Total liabilities and stockholders' equity	\$15,710				\$13,438			

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Net interest-earning assets	\$2,216			\$2,434	
Net interest income		\$ 97			\$ 77
Interest rate spread (3)		2.59	%	2.43	%
Net interest margin (4)		2.77	%	2.63	%
Ratio of average interest-earning assets to interest-bearing liabilities		118.8	%	126.4	%

(1) Includes nonaccrual loans, for further information relating to nonaccrual loans, see Note 4 - Loans

(1) Held-for-Investment.

(2) Includes noninterest-bearing company controlled deposits that arise due to the servicing of loans for others.

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

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

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	Six Months Ended June 30,				2016			
	2017		Annualized		Average		Annualized	
	Average	Interest	Yield/	%	Average	Interest	Yield/	%
	Balance	Rate	Rate		Balance	Rate	Rate	
	(Dollars in millions)							
Interest-Earning Assets								
Loans held-for-sale	\$3,780	\$ 74	3.94	%	\$2,897	\$ 54	3.72	%
Loans held-for-investment								
Residential first mortgage	2,447	41	3.35	%	2,504	39	3.12	%
Home equity	436	11	5.01	%	497	13	5.36	%
Other	26	—	4.52	%	29	1	4.94	%
Total Consumer loans	2,909	52	3.61	%	3,030	53	3.50	%
Commercial Real Estate	1,399	28	3.99	%	862	15	3.38	%
Commercial and Industrial	855	20	4.67	%	585	12	4.03	%
Warehouse Lending	770	18	4.62	%	1,141	25	4.29	%
Total Commercial loans	3,024	66	4.34	%	2,588	52	3.93	%
Total loans held-for-investment (1)	5,933	118	3.98	%	5,618	105	3.70	%
Loans with government guarantees	318	7	4.34	%	460	7	3.18	%
Investment securities	3,090	39	2.54	%	2,625	34	2.59	%
Interest-earning deposits	66	1	0.97	%	155	—	0.50	%
Total interest-earning assets	13,187	239	3.63	%	11,755	200	3.39	%
Other assets	1,694				1,736			
Total assets	\$14,881				\$13,491			
Interest-Bearing Liabilities								
Retail deposits								
Demand deposits	\$509	\$ —	0.17	%	\$463	\$ —	0.15	%
Savings deposits	3,930	15	0.76	%	3,706	15	0.79	%
Money market deposits	258	1	0.44	%	303	1	0.45	%
Certificates of deposit	1,083	6	1.07	%	904	4	0.96	%
Total retail deposits	5,780	22	0.75	%	5,376	20	0.74	%
Government deposits								
Demand deposits	217	—	0.39	%	230	—	0.39	%
Savings deposits	435	1	0.54	%	409	1	0.52	%
Certificates of deposit	305	1	0.65	%	411	1	0.71	%
Total government deposits	957	2	0.54	%	1,050	2	0.57	%
Wholesale deposits and other	6	—	0.42	%	—	—	—	%
Total interest-bearing deposits	6,743	24	0.72	%	6,426	22	0.70	%
Short-term Federal Home Loan Bank advances and other	2,630	12	0.89	%	1,249	3	0.40	%
Long-term Federal Home Loan Bank advances	1,200	11	1.89	%	1,592	15	1.91	%
Other long-term debt	493	12	5.05	%	247	4	3.27	%
Total interest-bearing liabilities	11,066	59	1.08	%	9,514	44	0.93	%
Noninterest-bearing deposits (2)	2,024				1,915			
Other liabilities	409				479			
Stockholders' equity	1,382				1,583			
Total liabilities and stockholders' equity	\$14,881				\$13,491			
Net interest-earning assets	\$2,121				\$2,241			
Net interest income		\$ 180				\$ 156		
Interest rate spread (3)			2.55	%			2.46	%
Net interest margin (4)			2.72	%			2.64	%

Ratio of average interest-earning assets to interest-bearing liabilities	119.2 %	123.6 %
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- (1) Includes nonaccrual loans, for further information relating to nonaccrual loans, see Note 4 - Loans Held-for-Investment.
- (2) Includes noninterest-bearing company controlled deposits that arise due to the servicing of loans for others.
- (3) Interest rate spread is the difference between rates of interest earned on interest-earning assets and rates of interest paid on interest-bearing liabilities.
- (4) Net interest margin is net interest income divided by average interest-earning assets.

Rate/Volume Analysis

The following tables present the dollar amount of changes in interest income and interest expense for the components of interest-earning assets and interest-bearing liabilities that are presented in the preceding table. The tables below distinguish between the changes related to average outstanding balances (changes in volume while holding the initial rate constant) and the changes related to average interest rates (changes in average rates while holding the initial balance constant). The rate/volume variances are allocated to variances due to rate.

	Three Months Ended June 30, 2017 Versus 2016 Increase (Decrease) Due to:		
	Rate	Volume	Total
	(Dollars in millions)		
Interest-Earning Assets			
Loans held-for-sale	\$4	\$ 12	\$16
Loans held-for-investment			
Total Consumer loans	1	2	3
Commercial Real Estate	3	5	8
Commercial and Industrial	2	3	5
Warehouse Lending	1	(5)	(4)
Total Commercial loans	6	3	9
Total loans held-for-investment	7	5	12
Loans with government guarantees	—	(1)	(1)
Investment securities	(1)	4	3
Total interest-earning assets	\$10	\$ 20	\$30
Interest-Bearing Liabilities			
Retail deposits	\$—	\$ 1	\$1
Government deposits	1	(1)	—
Short-term Federal Home Loan Bank advances and other	5	2	7
Long-term Federal Home Loan Bank advances	—	(2)	(2)
Other long-term debt	2	2	4
Total interest-bearing liabilities	8	2	10
Change in net interest income	\$2	\$ 18	\$20

	Six Months Ended June 30, 2017 Versus 2016 Increase (Decrease) Due to:		
	Rate	Volume	Total
	(Dollars in millions)		
Interest-Earning Assets			
Loans held-for-sale	\$4	\$ 16	\$20
Loans held-for-investment			
Residential first mortgage	3	(1)	2
Home equity	—	(2)	(2)
Other	(1)	—	(1)
Total Consumer loans	2	(3)	(1)
Commercial Real Estate	4	9	13
Commercial and Industrial	3	5	8
Warehouse Lending	1	(8)	(7)
Total Commercial loans	8	6	14
Total loans held-for-investment	10	3	13
Loans with government guarantees	2	(2)	—
Investment securities	(1)	6	5
Interest-earning deposits	1	—	1
Total interest-earning assets	\$16	\$ 23	\$39
Interest-Bearing Liabilities			
Retail deposits	\$(1)	\$ 3	\$2
Short-term Federal Home Loan Bank advances and other	6	3	9
Long-term Federal Home Loan Bank advances	—	(4)	(4)
Other long-term debt	4	4	8
Total interest-bearing liabilities	9	6	15
Change in net interest income	\$7	\$ 17	\$24

Comparison to Prior Year Quarter

Net interest income increased \$20 million or 26 percent for the three months ended June 30, 2017, compared to the same period in 2016. This increase was primarily driven by an increase in average rates and growth in interest-earning assets. This was partially offset by an increase in average rates and the average balance of borrowings, resulting from an increase in the Federal Reserve rates and the third quarter 2016 issuance of \$250 million of 6.125 percent senior notes ("2021 Senior Notes") which were issued to fund the redemption of our TARP Preferred.

Our net interest margin for the three months ended June 30, 2017 was 2.77 percent, compared to 2.63 percent for the three months ended June 30, 2016. The net 14 basis point increase was driven by higher interest income on LHFS due to increases in market rates and an increase in higher yielding commercial loans within the LHFI portfolio. This increase was partially offset by higher average rates on short-term FHLB advances and the third quarter 2016 debt issuances.

For the three months ended June 30, 2017 as compared to the three months ended June 30, 2016, total interest earning assets increased \$2.4 billion to \$14.0 billion led by growth in LHFS primarily due to extending turn times and the accumulation of loans in support of a residential mortgage backed securitization that closed in the third quarter 2017, as well as higher mortgage originations. Additionally, the \$440 million increase in average commercial loans was consistent with our strategy to grow the community bank and enhance the yield on our interest-earning assets.

Average interest-bearing liabilities increased \$2.6 billion for the three months ended June 30, 2017, compared to the three months ended June 30, 2016. The increase was primarily driven by a \$2.6 billion increase in short-term FHLB advances to fund balance sheet growth.

Comparison to Prior Year to Date

Net interest income increased \$24 million for the six months ended June 30, 2017, compared to the same period in 2016, primarily driven by growth in interest-earning assets and an increase in average rates. This was partially offset by an increase in average rates and average balances of our borrowings, resulting from the third quarter 2016 issuance of 2021 Senior Notes which were issued to fund the redemption of our TARP Preferred.

Our net interest margin for the six months ended June 30, 2017 was 2.72 percent, compared to 2.64 percent for the six months ended June 30, 2016. The net 8 basis point increase was positively impacted by an increase in market rates, higher yielding commercial loan portfolio and stable deposit costs. This improvement was partially offset by higher rates on short-term FHLB advances driven by recent Federal Reserve rate increases and the issuance of our 2021 Senior Notes in the third quarter 2016.

For the six months ended June 30, 2017 as compared to the six months ended June 30, 2016, average interest earning assets increased \$1.4 billion, led by a \$883 million increase in LHFS due to extending turn times and higher mortgage activity. The combined \$901 million increase in average commercial loans and average investment securities was consistent with our strategy to grow the community bank and enhance the yield on our interest-earning assets. Commercial loans increased 17 percent due to growth in the commercial real estate and commercial & industrial portfolios.

Average interest-bearing liabilities increased \$1.6 billion for the six months ended June 30, 2017, compared to the six months ended June 30, 2016. The increase was driven by a \$1.4 billion increase in FHLB advances used to fund balance sheet growth and the issuance of our 2021 Senior Notes in the third quarter 2016.

Provision (Benefit) for Loan Losses

Credit Quality Ratios

	Three Months Ended June 30, 2017			Six Months Ended June 30, 2017		
	2017	2016	Change	2017	2016	Change
Charge-offs, net of recoveries	\$—	\$9	\$(9)	\$4	\$21	\$(17)
Charge-offs associated with loans with government guarantees	—	4	(4)	2	7	(5)
Charge-offs associated with the sale or transfer of nonperforming loans and TDRs	—	2	(2)	1	8	(7)
Charge-offs, net of recoveries, adjusted (1)	\$—	\$3	\$(3)	\$1	\$6	\$(5)
Net charge-offs to LHFI ratio (annualized)	0.04%	0.62%	(0.58)%	0.15%	0.74%	(0.59)%
Net charge-off ratio, adjusted (annualized)(1)	0.02%	0.18%	(0.16)%	0.02%	0.44%	(0.42)%

(1) Excludes charge-offs associated with loans with government guarantees and charge-offs associated with the sale or transfer of nonperforming loans and TDRs.

Comparison to Prior Year Quarter

The provision (benefit) for loan losses was a benefit of \$1 million during the three months ended June 30, 2017, compared to a benefit of \$3 million during the three months ended June 30, 2016. During the three months ended June 30, 2017, the \$1 million benefit reflects continued low level of losses and strong credit quality of our loan portfolios. The \$3 million benefit during the three months ended June 30, 2016 resulted primarily from reserves that were released in conjunction with the sale of \$408 million UPB of performing residential first mortgage loans.

As a result of the strong credit quality throughout our loan portfolios, net charge-offs for the three months ended June 30, 2017 decreased to less than \$1 million, compared to \$9 million for the three months ended June 30, 2016. As a percentage of the average LHFI, net charge-offs for the three months ended June 30, 2017, decreased to 0.04 percent from 0.62 percent for the three months ended June 30, 2016.

Comparison to Prior Year to Date

The provision (benefit) for loan losses was a provision of \$2 million for the six months ended June 30, 2017, compared to a benefit of \$16 million during the six months ended June 30, 2016. The \$2 million provision for the six months ended June 30, 2017, resulted primarily from \$4 million in net charge-offs partially offset by a reduction in reserve, reflective of the continued strong credit quality of our loan portfolios and low level of net losses. The \$16 million benefit for the six

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months ended June 30, 2016 resulted primarily from the sale of \$1.2 billion UPB of performing residential first mortgage loans and \$110 million UPB of nonperforming, TDR and non-agency loans.

Net charge-offs for the six months ended June 30, 2017 decreased to \$4 million, compared to \$21 million for the six months ended June 30, 2016. As a percentage of the average LHFI, net charge-offs for the six months ended June 30, 2017 decreased to 0.15 percent from 0.74 percent for the three months ended June 30, 2016, partially driven from loan sales of \$110 million UPB of nonperforming loans which occurred in the first half of 2016.

For further information on the provision for loan losses see MD&A - Allowance for Loan Losses.

Noninterest Income

The following tables provide information on our noninterest income along with additional details related to our net gain on loan sales and other mortgage metrics:

	Three Months Ended June 30,			Six Months Ended June 30,		
	2017	2016	Change	2017	2016	Change
	(Dollars in millions)					
Net gain on loan sales	\$66	\$90	\$ (24)	\$114	\$165	\$ (51)
Loan fees and charges	20	19	1	35	34	1
Deposit fees and charges	5	6	(1)	9	12	(3)
Loan administration income	6	4	2	11	10	1
Net (loss) return on mortgage servicing rights	6	(4)	10	20	(10)	30
Representation and warranty benefit	3	4	(1)	7	6	1
Other noninterest income	10	9	1	20	16	4
Total noninterest income	\$116	\$128	\$ (12)	\$216	\$233	\$ (17)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(Dollars in millions)			
Mortgage rate lock commitments (fallout-adjusted) (1)	\$9,002	\$8,127	\$14,998	\$14,990
Net margin on mortgage rate lock commitments (fallout-adjusted) (1) (2)	0.73 %	1.04 %	0.76 %	1.00 %
Gain on loan sales LHFS + net (loss) return on the MSR	\$72	\$81	\$134	\$141
Mortgage loans sold and securitized	8,989	7,940	13,473	14,888
Net margin on loans sold and securitized	0.73 %	1.07 %	0.84 %	1.01 %

(1) Fallout adjusted refers to mortgage rate lock commitments which are adjusted by a percentage of mortgage loans in the pipeline that are not expected to close based on our historical experience and the level of interest rates.

(2) Gain on sale margin is based on net gain on loan sales related to LHFS to fallout-adjusted mortgage rate lock commitments.

Comparison to Prior Year Quarter

Total noninterest income decreased \$12 million during the three months ended June 30, 2017, compared to the same period in 2016.

Net gain on loan sales decreased \$24 million during the three months ended June 30, 2017, compared to the three months ended June 30, 2016. The net gain on loan sales margin decreased 34 basis points primarily driven by our

decision to extend turn times on LHFS which shifts earnings from gain on sale to net interest income, and a shift in mix and shorter-term market forces. The decrease in net gain on loan sales was also attributed to the sale of performing LHFIs that occurred in the second quarter of 2016 which resulted in a \$5 million gain. The decreases were partially offset by \$875 million in higher fallout-adjusted locks driven by recent acquisitions.

Net return on MSR (including the impact of economic hedges) was \$6 million for the three months ended June 30, 2017, compared to a loss of \$4 million during the three months ended June 30, 2016. The \$10 million increase was primarily driven by a more stable prepayment environment and improvements in our hedging program, partially offset by higher transaction costs and lower servicing fees resulting from a lower MSR balance driven by MSR sales that occurred in the second quarter 2017.

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Comparison to Prior Year to Date

Total noninterest income decreased \$17 million during the six months ended June 30, 2017, compared to the same period in 2016.

Net gain on loan sales decreased \$51 million during the six months ended June 30, 2017, compared to the six months ended June 30, 2016. The net gain on loan sales margin decreased 17 basis points primarily driven by our decision to extend turn times on LHFS which shifts earnings from gain on sale to net interest income, and a shift in mix and shorter-term market forces. The decrease in net gain on loan sales was also attributed to the sale of performing LHFI that occurred in the first half of 2016 which resulted in a \$14 million gain.

Deposit fees and charges decreased \$3 million during the six months ended June 30, 2017, compared to the six months ended June 30, 2016. The decrease was primarily due to lower exchange fee income resulting from limitations set by the Durbin amendment, which became applicable to the Bank on July 1, 2016.

Net return on MSR was \$20 million for the six months ended June 30, 2017, compared to a loss of \$10 million during the six months ended June 30, 2016. The \$30 million increase was primarily driven by a more stable prepayment environment and improvements in our hedging program, partially offset by lower servicing fee income and higher transaction costs resulting from a lower MSR balance driven by MSR sales that occurred in 2017.

Other noninterest income increased \$4 million during the six months ended June 30, 2017, compared to the six months ended June 30, 2016. The increase was primarily due to favorable adjustments related to assets and liabilities held at fair value.

Noninterest Expense

The following table sets forth the components of our noninterest expense:

	Three Months			Six Months		
	Ended June 30,		Change	Ended June 30,		Change
	2017	2016		2017	2016	
	(Dollars in millions)					
Compensation and benefits	\$71	\$66	\$ 5	\$143	\$134	\$ 9
Commissions	16	14	2	26	24	2
Occupancy and equipment	25	21	4	47	43	4
Loan processing expense	14	15	(1)	26	27	(1)
Legal and professional expense	8	6	2	15	15	—
Other noninterest expense	20	17	3	37	33	4
Total noninterest expense	\$154	\$139	\$ 15	\$294	\$276	\$ 18
Efficiency ratio	72.0 %	68.2 %	3.8 %	74.2 %	71.2 %	3.0 %

Comparison to Prior Year Quarter

Noninterest expense increased \$15 million to \$154 million during the three months ended June 30, 2017, compared to \$139 million during the three months ended June 30, 2016. This is primarily due to an increase in compensation and benefits resulting from an increase in headcount to support growth initiatives. The three months ended June 30, 2017 included \$11 million of operating expenses and \$1 million of transaction costs related to the recent acquisitions. The increase was further impacted by an increase in occupancy and equipment primarily due to a higher asset base.

Comparison to Prior Year to Date

Noninterest expense increased \$18 million to \$294 million during the six months ended June 30, 2017, compared to \$276 million during the six months ended June 30, 2016. The increase was primarily driven by higher compensation and benefits which was the result of an increase in headcount due to recent growth initiatives. The six months ended June 30, 2017 included \$11 million of operating expenses and \$2 million of transaction costs related to the recent acquisitions. The remaining increase was primarily driven by higher occupancy and equipment due to a higher asset base and higher other noninterest expenses driven by an increase in advertising related to a direct mail campaign and new branding initiatives.

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Provision (benefit) for Income Taxes

Our provision for income taxes for the three and six months ended June 30, 2017 was \$19 million and \$32 million, respectively, compared to a provision of \$22 million and \$43 million during the three and six months ended June 30, 2016, respectively.

Our effective tax rate for the three and six months ended June 30, 2017 was 31.8 percent and 32.3 percent, respectively, compared to 32.7 percent and 33.4 percent for the three and six months ended June 30, 2016, respectively.

Our effective tax rate for the three and six months ended June 30, 2017 differs from the combined federal and state statutory tax rate primarily due to a benefit from tax-exempt earnings, partially offset by nondeductible expenses.

For further information, see Note 14 - Income Taxes.

OPERATING SEGMENTS

Overview

For detail on each segment's objectives, strategies, and priorities, please read this section in conjunction with Note 18 - Segment Information, and other sections of this report for a full understanding of our consolidated financial performance.

The net income (loss) by operating segment is presented in the following table:

	Three Months Ended June 30, 2017			Six Months Ended June 30, 2016			Change		
	2017	2016	Change	2017	2016	Change	2017	2016	Change
	(Dollars in millions)								
Community Banking	\$10	\$9	\$ 1	\$16	\$27	\$(11)			
Mortgage Originations	30	38	(8)	56	60	(4)			
Mortgage Servicing	(3)	(2)	(1)	(8)	(6)	(2)			
Other	4	2	2	4	5	(1)			
Total net income	\$41	\$47	\$ (6)	\$68	\$86	\$(18)			

Community Banking

Comparison to Prior Year Quarter

During the three months ended June 30, 2017, the Community Banking segment reported net income of \$10 million, compared to \$9 million for the three months ended June 30, 2016. The increase in net income was primarily due to \$8 million higher net interest income from higher average loan balances, led by growth in commercial loans and higher average loan yields. These increases were partially offset by a \$3 million increase in the provision for loan losses resulting from loan growth and a decrease of \$4 million in gain on loan sales, primarily resulting from second quarter 2016 sale of performing LHFI.

Comparison to Prior Year to Date

During the six months ended June 30, 2017, the Community Banking segment reported net income of \$16 million, compared to \$27 million for the six months ended June 30, 2016. The \$11 million decrease in net income was primarily due to a \$12 million decrease in gain on loan sales and an \$18 million increase in the provision for loan losses. For the six months ended June 30, 2016, the provision for loan losses was a \$16 million benefit primarily resulting from the sale of \$1.2 billion of performing LHFIs sold from the Community Bank loan portfolio, compared to a provision of \$2 million in first six months of 2017. This decrease in net income was partially offset by a \$12 million increase in net interest income resulting from loan growth and higher yields.

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Mortgage Originations

Comparison to Prior Year Quarter

The Mortgage Originations segment net income decreased \$8 million to \$30 million during the three months ended June 30, 2017, compared to \$38 million in the three months ended June 30, 2016. The decrease was primarily due to a \$20 million decrease in net gain on loan sales driven by a 31 basis point decrease in margin resulting from a more competitive market and the impact of extending turn times on LHFS which shifts earnings from gain on sale to net interest income. The benefit of extended turn times, as well as higher mortgage originations, resulted in an \$11 million increase in interest income. Net return on the MSRs increased \$10 million driven by an increase in the interest rate environment experienced in the second quarter of 2017 which resulted in lower prepayments and favorable fair value adjustments. Noninterest expense increased \$13 million for the three months ended June 30, 2017 compared to the three months ended June 30, 2016, primarily due to increases in compensation and benefits and acquisition costs, along with an increase in commissions due to increased loan production.

Comparison to Prior Year to Date

The Mortgage Originations segment net income decreased \$4 million to \$56 million during the six months ended June 30, 2017, compared to \$60 million in the six months ended June 30, 2016. The decrease was primarily due to a \$39 million decrease in net gain on loan sales driven by a 22 basis point decrease in margin, resulting from a more competitive market and the impact of extending turn times on LHFS which shifts earnings from gain on sale to net interest income. The decrease was partially offset by a \$30 million increase in net return on the MSR resulting from an increase in the interest rate environment in 2017 which resulted in lower prepayments and favorable fair value adjustments. Net interest income increased \$19 million resulting from an increase in mortgage activity and the impact of extending turn times on LHFS. Noninterest expense increased \$16 million for the six months ended June 30, 2017 compared to the six months ended June 30, 2016, primarily due to increases in compensation and benefits and acquisition costs, along with an increase in commissions due to increased loan production.

Mortgage Servicing

Comparison to Prior Year Quarter

The Mortgage Servicing segment reported a net loss of \$3 million for the three months ended June 30, 2017, compared to a net loss of \$2 million for the three months ended June 30, 2016. The increase on net losses is primarily due to an increase in compensation and benefits driven by an increase in headcount.

Comparison to Prior Year to Date

The Mortgage Servicing segment reported a net loss of \$8 million for the six months ended June 30, 2017, compared to a net loss of \$6 million for the six months ended June 30, 2016. The increase in net losses is primarily due to an increase in compensation and benefits driven by an increase in headcount.

Other

Comparison to Prior Year Quarter

For the three months ended June 30, 2017, the Other segment net income was \$4 million, compared to net income of \$2 million for the three months ended June 30, 2016. The \$2 million improvement was primarily due to an increase in

net interest income resulting from higher average investment balances, due to pulling ahead planned purchases of investments to take advantage of a higher return market.

Comparison to Prior Year to Date

For the six months ended June 30, 2017, the Other segment net income was \$4 million, compared to net income of \$5 million for the six months ended June 30, 2016. The \$1 million decrease was primarily due to a reduction in net interest income, as a result of higher interest expense due to our issuance of our 2021 Senior Notes, which occurred in the third quarter of 2016.

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Condensed Consolidated Balance Sheet Review

	June 30, 2017	December 31, 2016	Change
	(Dollars in millions)		
Assets			
Total cash and cash equivalents	\$183	\$158	\$25
Investment Securities	2,628	2,573	55
Loans held-for-sale	4,506	3,177	1,329
Loans held-for-investment	6,776	6,065	711
Loans with government guarantees	278	365	(87)
Less: allowance for loan losses	(140)	(142)	2
Total loans held-for-investment and loans with government guarantees, net	6,914	6,288	626
Mortgage servicing rights	184	335	(151)
Other assets	1,550	1,522	28
Total assets	\$15,965	\$14,053	\$1,912
Liabilities and Stockholders' Equity			
Total deposits	\$8,695	\$8,800	\$(105)
Federal Home Loan Bank advances	4,870	2,980	1,890
Other long-term debt	493	493	—
Other Liabilities	499	444	55
Total liabilities	14,557	12,717	1,840
Total stockholders' equity	1,408	1,336	72
Total liabilities and stockholders' equity	\$15,965	\$14,053	\$1,912

At June 30, 2017 our assets totaled \$16.0 billion, up \$1.9 billion from December 31, 2016. Asset growth was attributable to an increase in our LHFS as a result of higher mortgage volumes as well as growth in our commercial and consumer LHFI portfolios. Total liabilities increased to \$14.6 billion at June 30, 2017 due to an increase in FHLB advances to primarily support the growth of our LHFS.

Loans held-for-sale

The majority of our mortgage loans originated as LHFS are sold into the secondary market by securitizing the loans into agency mortgage backed securities or on a whole loan basis. Sales of loans totaled \$9.0 billion, or 97.7 percent of originations during the three months ended June 30, 2017, compared to \$7.9 billion, or 95.3 percent of originations during the three months ended June 30, 2016. The increase in sales volume and percentage of originations during the three months ended June 30, 2017, as compared to the three months ended June 30, 2016, was primarily due to recent acquisitions. During the three months ended June 30, 2017, turn times on sales of LHFS were an average of 44 days compared to an average of 30 days during the three months ended June 30, 2016 which benefits net interest income.

As of June 30, 2017, we had outstanding commitments to sell \$6.7 billion of mortgage loans. Generally, these commitments are funded within 120 days. At June 30, 2017 and December 31, 2016, consumer LHFS totaled \$4.5 billion and \$3.2 billion, respectively, which are primarily residential mortgage loans. The \$1.3 billion increase is the result of higher mortgage activity and the accumulation of loans in support of a residential mortgage backed securitization that closed in the third quarter 2017.

On July 31, 2017, the Company closed on a securitization of \$444 million of residential mortgage-backed certificates (RMBS) issued by Flagstar Mortgage Trust 2017-1 (FSMT 2017-1). The pool comprises loans Flagstar originated through its retail, broker and correspondent channels. The collateral pool consists of high-quality 30- and 15-year, fully amortizing high balance conforming and jumbo fixed-rate Safe Harbor Qualified Mortgage loans to borrowers

with strong credit profiles and low leverage.

For further information, see Note 3 - Loans Held-for-Sale.

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Loans held-for-investment

Loans held-for-investment are summarized as follows:

	June 30, 2017	December 31, 2016	Change
(Dollars in millions)			
Consumer loans			
Residential first mortgage	\$2,538	\$ 2,327	\$ 211
Home equity	459	443	16
Other	27	28	(1)
Total consumer loans	3,024	2,798	226
Commercial loans			
Commercial real estate (1)	1,557	1,261	296
Commercial and industrial	1,040	769	271
Warehouse lending	1,155	1,237	(82)
Total commercial loans	3,752	3,267	485
Total loans held-for-investment	\$6,776	\$ 6,065	\$ 711

(1) Includes \$253 million and \$245 million of owner occupied commercial real estate loans at June 30, 2017 and December 31, 2016, respectively.

Loans held-for-investment increased \$711 million, at June 30, 2017 from December 31, 2016. This increase was due to growth in both our consumer loan portfolio and commercial loan portfolio.

We have continued strong commercial loan growth as a result of our strategic initiative to grow the Community Bank and improve margins by adding higher yielding loans. The commercial loan portfolio has increased \$485 million, or 15 percent, since December 31, 2016. During the six months ended June 30, 2017, our CRE LHFH portfolio grew \$296 million and C&I \$271 million.

For further information, see Note 4 - Loans Held-for-Investment.

Loans with government guarantees

Our loans with government guarantees portfolio totaled \$278 million at June 30, 2017, as compared to \$365 million at December 31, 2016. The decrease is primarily due to loans transferred to HFS and resold to Ginnie Mae out-pacing new repurchases.

For further information, see Note 5 - Loans with Government Guarantees.

Allowance for loan losses

The ALLL decreased \$2 million to \$140 million at June 30, 2017, compared to \$142 million at December 31, 2016. The decrease from December 31, 2016 was driven by continued low charge-off levels along with the strong credit quality of the loans within our LHFH portfolios.

For further information, see MD&A Risk Management - Allowance for Loan Losses.

Mortgage servicing rights

At June 30, 2017, MSRs decreased \$151 million to \$184 million, compared to \$335 million at December 31, 2016, primarily due to MSR bulk sales of \$22.9 billion in underlying loans, partially offset by additions from loan sales where we retained servicing. In the first half of 2017, we sold MSRs with a fair value of \$256 million, successfully executing our MSR reduction strategy to release capital and support balance sheet growth.

The principal balance of the loans underlying our total MSRs was \$16.1 billion at June 30, 2017, compared to \$31.2 billion at December 31, 2016 with the decrease primarily attributable to MSR bulk sales in the first six months of 2017, partially offset by loan sales where we retained servicing.

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For further information, see MD&A Risk Management - Capital and Note 7 - Mortgage Servicing Rights.

Deposits

The composition of our deposits was as follows:

	June 30, 2017		December 31, 2016		Change
	Balance	% of Deposits	Balance	% of Deposits	
(Dollars in millions)					
Retail deposits					
Branch retail deposits					
Demand deposit accounts	\$899	10.3 %	\$852	9.7 %	\$47
Savings accounts	3,836	44.1 %	3,824	43.5 %	12
Money market demand accounts	131	1.5 %	138	1.6 %	(7)
Certificates of deposit/CDARS (1)	1,102	12.7 %	1,055	12.0 %	47
Total branch retail deposits	5,968	68.6 %	5,869	66.7 %	99
Commercial retail deposits					
Demand deposit accounts	331	3.8 %	282	3.2 %	49
Savings accounts	80	0.9 %	63	0.7 %	17
Money market demand accounts	117	1.3 %	109	1.2 %	8
Certificates of deposit/CDARS (1)	51	0.6 %	1	— %	50
Total commercial retail deposits	579	6.7 %	455	5.2 %	124
Total retail deposits	\$6,547	75.3 %	\$6,324	71.9 %	\$223
Government deposits					
Demand deposit accounts	\$204	2.3 %	\$250	2.8 %	\$(46)
Savings accounts	361	4.2 %	451	5.1 %	(90)
Certificates of deposit/CDARS (1)	286	3.3 %	329	3.7 %	(43)
Total government deposits (2)	851	9.8 %	1,030	11.7 %	(179)
Company controlled deposits (3)	1,297	14.9 %	1,446	16.4 %	(149)
Total deposits (4)	\$8,695	100.0 %	\$8,800	100.0 %	\$(105)

(1) The aggregate amount of certificates of deposit with a minimum denomination of \$100,000 was approximately \$1.1 billion and \$1.0 billion at June 30, 2017 and December 31, 2016.

(2) Government deposits include funds from municipalities and schools.

(3) These accounts represent a portion of the investor custodial accounts and escrows controlled by us in connection with loans serviced for others and that have been placed on deposit with the Bank.

(4) The aggregate amount of deposits with a balance over \$250,000 was approximately \$4.0 billion at both June 30, 2017 and December 31, 2016.

Total deposits decreased \$105 million, or 1.2 percent at June 30, 2017, compared to December 31, 2016, primarily due to a decline of \$179 million in government deposits and \$149 million in company controlled deposits. This decline was partially offset by a \$223 million, or 3.5 percent increase in retail deposits led by increases in demand deposits and certificates of deposit. The increase in retail deposits demonstrates our strategic initiatives to drive deposit growth by bringing in deposits from commercial customers.

Federal Home Loan Bank advances

Federal Home Loan Bank advances. FHLB advances increased \$1.9 billion to \$4.9 billion at June 30, 2017 from \$3.0 billion at December 31, 2016, due to short term advances funding loan growth, primarily in the LHFS portfolio.

For further information, see MD&A Risk Management - Liquidity Risk and Note 9 - Borrowings.

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RISK MANAGEMENT

Like all financial services companies, we engage in business activities and assume the related risks. The risks we are subject to in the normal course of business include, but are not limited to, credit, regulatory compliance, legal, reputation, liquidity, market, operational, and strategic. We have made significant investments in our risk management activities which are focused on ensuring we properly identify, measure and manage such risks across the entire enterprise to maintain safety and soundness and maximize profitability. We hold capital to protect from the risk of unexpected loss.

A comprehensive discussion of risks affecting us can be found in the Risk Factors section included in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2016. Some of the more significant processes used to manage and control credit, liquidity, market, and operational risks are described in the following paragraphs.

Credit Risk

Credit risk is the risk of loss to us arising from an obligor's inability or failure to meet contractual payment or performance terms. Like other financial services institutions, we provide loans, extend credit, purchase securities, and enter into financial derivative contracts, all of which have related credit risk. The majority of our credit risk is associated with lending activities, as the acceptance and management of credit risk is central to profitable lending.

Flagstar maintains a strict credit limit, in compliance with regulatory requirements, in order to maintain a diversified loan portfolio and manage its credit exposure to any one borrower or obligor. Under the Home Owners Loan Act ("HOLA"), savings associations are generally subject to national bank limits on loans to one borrower. Generally, per HOLA, the Bank may not make a loan or extend credit to a single or related group of borrowers in excess of 15 percent of Tier 1 and Tier 2 capital plus any portion of the allowance for loan losses not included in the Tier 2 capital, which was \$260 million as of June 30, 2017. Flagstar maintains a maximum internal Bank limit of \$100 million (commitment level) to any one borrower/obligor relationship, which is more conservative than the limit required by HOLA. All credit exposures that exceed \$50 million must be approved by the Board of Directors.

We manage our credit risk by establishing sound credit policies for underwriting and adhering to well controlled processes. We utilize various credit risk management and monitoring activities to mitigate risks associated with loans that we hold, acquire, and originate.

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Residential first mortgage loans. We originate or purchase various types of conforming and non-conforming fixed and adjustable rate loans underwritten using Fannie Mae and Freddie Mac guidelines for the purpose of purchasing or refinancing owner occupied and second home properties. The LTV requirements vary depending on occupancy, property type, loan amount, and FICO. Loans with LTVs exceeding 80 percent are required to obtain mortgage insurance.

The following table presents our total residential first mortgage LHFI by major category:

	June 30, 2017	December 31, 2016
	(Dollars in millions)	
Current estimated LTV ratios		
Less than 80% and refreshed FICO scores (1):		
Equal to or greater than 660	\$2,279	\$ 2,077
Less than 660	87	95
80% and greater and refreshed FICO scores (1):		
Equal to or greater than 660	102	78
Less than 660	8	9
U.S. government guaranteed	62	68
Total	\$2,538	\$ 2,327
Geographic region		
California	\$992	\$ 858
Michigan	250	236
Florida	197	193
Texas	162	138
Washington	148	136
Illinois	93	84
New York	71	68
Arizona	70	65
Colorado	63	60
Maryland	63	59
Others	429	430
Total	\$2,538	\$ 2,327

(1)Current FICO scores, which are updated one month prior to each quarter end, have been updated as of May 30, 2017, where available, or as of the most recent credit score.

Home equity. Our home equity portfolio includes second mortgages, HELOANs and HELOCs. These loans require full documentation and are underwritten and priced to ensure high credit quality and loan profitability. Our debt-to-income ratio on second mortgages is capped at 43 percent and for HELOCs is capped at 45 percent. We currently limit the maximum CLTV to 89.99 percent and FICO scores to a minimum of 660. Current second mortgage loans/HELOANS are fixed rate loans and are available with terms up to 15 years. HELOC loans are adjustable-rate loans that contain a 10-year interest-only draw period followed by a 20-year amortizing period.

Commercial and industrial loans. Commercial and industrial LHFI facilities typically include lines of credit and term loans to middle market businesses for use in normal business operations to finance working capital, equipment and capital purchases, acquisition and expansion projects. We lend to customers with a history of profitability and a long-term business model. Generally, leverage is limited to a ratio of 3 times and the minimum debt service coverage

is 1.20. Most of our C&I loans earn interest at a variable rate and we offer our customers the ability to enter into interest rate swaps.

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The following table presents our total C&I LHFH by borrower's geographic concentration and industry type at June 30, 2017:

Industry Type	State							Total	% by industry
	Michigan	Florida	Texas	California	Ohio	Tennessee	Other		
	(Dollars in millions)								
Services (1)	\$99	\$ 1	\$62	\$ 39	\$—	\$ 39	\$110	\$350	33.7 %
Financial and insurance	72	56	—	—	52	6	105	291	28.0 %
Manufacturing	99	—	5	24	—	—	68	196	18.8 %
Distribution	55	—	—	2	—	—	—	57	5.5 %
Servicing advances	—	25	—	—	—	—	26	51	4.9 %
Rental & leasing	48	—	—	—	—	—	—	48	4.6 %
Government & education	11	—	—	—	—	—	36	47	4.5 %
Total	\$384	\$ 82	\$67	\$ 65	\$52	\$ 45	\$345	\$1,040	100.0 %
Percent by state	36.9 %	7.9 %	6.4 %	6.3 %	5.0 %	4.3 %	33.2 %	100.0 %	

(1) Includes unsecured home builder loans of \$80 million at June 30, 2017.

Commercial real estate loans. Our commercial real estate LHFH portfolio is comprised of loans that are collateralized by diversified real estate properties intended to be income-producing in the normal course of business. Our commercial real estate lending relationships are primarily based in the Midwest. Generally, the maximum LTV is 80 percent, or 85 percent for owner-occupied real estate, and debt service coverage of 1.20 to 1.35 times. This portfolio also includes owner occupied real estate loans, in addition to secured home builder loans. In 2016, we launched a national home builder finance program to grow our balance sheet, increase commercial deposits and develop incremental revenue through our retail purchase mortgage channel.

The following table presents our total CRE LHFH by borrower's geographic concentration and collateral type at June 30, 2017:

Collateral Type	State					Total (1)
	Michigan	Florida	Colorado	California	Other	
	(Dollars in millions)					
Single family residence, which includes land (2)	\$53	\$41	\$ 61	\$ 6	\$127	\$288
Retail (3)	185	33	—	9	12	239
Apartments	123	16	4	—	66	209
Office	149	—	—	19	—	168
Industrial	131	—	—	35	5	171
Hotel/motel	74	—	—	—	35	109
Land - Residential Development	12	18	25	6	28	89
Parking garage/Lot	67	—	—	—	—	67
Senior Living facility	44	—	—	9	—	53
Non Profit	38	—	—	—	8	46
Regional Mall (4)	25	—	—	—	—	25
Condominiums	9	—	—	—	16	25
Marina	23	—	—	—	—	23
Special Purposes and all other (5)	32	—	—	4	9	45
Total	\$965	\$108	\$ 90	\$ 88	\$306	\$1,557
Percent	62.0 %	6.9 %	5.8 %	5.7 %	19.7 %	100.0 %

(1) Includes \$253 million of commercial owner occupied real estate loans at June 30, 2017.

- (2) Includes \$311 million of secured home builder loans at June 30, 2017.
- (3) Includes multipurpose retail space, neighborhood centers, strip malls and single-use retail space.
- (4) Consists of one mall which includes an anchor store.
- (5) Special purposes and all other primarily includes: movie theaters, land (vacant), and mini storage facilities, etc.

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Warehouse lending. We also offer warehouse lines of credit to other mortgage lenders. These allow the lender to fund the closing of residential first mortgage loans. Each extension or draw-down on the line is fully collateralized by conforming mortgage loans and is paid off when the lender sells the loan to an outside investor or, in some instances, to the Bank. Underlying mortgage loans are predominantly originated using the agencies' underwriting standards. The guideline for debt to tangible net worth is 15 to 1. Despite the contraction in warehouse lending which occurred in the first quarter 2017, we are continuing to focus on increasing market share in the warehouse lending market through our strategic initiative to increase lending to customers who originate loans they then sell to outside third party investors. We have a national platform with relationship managers covering both coasts and a large Michigan-based sales team. The aggregate committed amount of adjustable-rate warehouse lines of credit granted to other mortgage lenders at June 30, 2017 was \$2.6 billion, of which \$1.2 billion was outstanding, compared to \$2.9 billion at December 31, 2016, of which \$1.2 billion was outstanding.

Credit Quality

Management considers a number of qualitative and quantitative factors in assessing the level of our ALLL. For further information see MD&A - Allowance for Loan Losses. As illustrated in the following tables, trends in certain credit quality characteristics such as nonperforming loans and past due statistics remain very strong and continue to show improvement. This is predominantly a result of run-off and sales of legacy portfolios that included nonperforming and TDR loans which have been replaced by new loans with strong credit characteristics.

The following table sets forth certain information about our nonperforming assets as of the end of each of the last five quarters:

	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016
	(Dollars in millions)				
Nonperforming LHFI	\$18	\$17	\$22	\$23	\$23
Nonperforming TDRs	5	5	8	8	6
Nonperforming TDRs at inception but performing for less than six months	7	6	10	9	15
Total nonperforming LHFI (1)	30	28	40	40	44
Real estate and other nonperforming assets, net	9	13	14	15	19
Nonperforming assets held-for-investment, net	\$39	\$41	\$54	\$55	\$63
Nonperforming assets to total assets	0.24%	0.27%	0.39%	0.39%	0.46%
Nonperforming LHFI to LHFI	0.44%	0.47%	0.67%	0.63%	0.76%
ALLL to LHFI (2)	2.07%	2.37%	2.37%	2.30%	2.62%
ALLL to LHFI and loans with government guarantees (2)	1.99%	2.25%	2.23%	2.16%	2.43%
Net charge-offs to LHFI ratio (annualized) (2)	0.04%	0.27%	0.13%	0.51%	0.62%
Nonperforming assets to LHFI and repossessed assets	0.57%	0.69%	0.90%	0.87%	1.09%
Nonperforming assets to Tier 1 capital (to adjusted total assets) + ALLL (3)	2.51%	2.90%	3.93%	4.03%	3.79%

(1) Does not include nonperforming LHFS of \$7 million, \$21 million, \$6 million, \$5 million and \$5 million at June 30, 2017, March 31, 2017, December 31, 2016, September 30, 2016 and June 30, 2016, respectively.

(2) Excludes loans carried under the fair value option.

(3) Refer to MD&A - Use of Non-GAAP Financial Measures for calculation of ratio.

Past due loans held-for-investment

For all loan categories within the consumer and commercial loan portfolio, loans are placed on nonaccrual status when any portion of principal or interest is 90 days past due (or nonperforming), or earlier when we become aware of information indicating that collection of principal and interest is in doubt. While it is the goal of management to collect on loans, we attempt to work out a satisfactory repayment schedule or modification with past due borrowers and will undertake foreclosure proceedings if the delinquency is not satisfactorily resolved. Our practices regarding past due loans are designed to both assist borrowers in meeting their contractual obligations and minimize losses incurred by the bank. When a loan is placed on nonaccrual status, the accrued interest income is reversed. Loans return to accrual status when principal and interest become current and are anticipated to be fully collectible.

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The following table sets forth information regarding past due LHFI at the dates listed:

	30 Days Past Due	60 – 90 Days Past Due	or Greater Past Due (1)	Total Past Due
(Dollars in millions)				
June 30, 2017				
Consumer Loans				
Residential First Mortgage	\$1	\$3	\$25	\$29
Home equity	1	—	5	6
Total Consumer Loans	2	3	30	35
Commercial loans				
Commercial real estate	1	—	—	1
Total commercial loans	1	—	—	1
Total Loans	\$3	\$3	\$30	\$36

December 31, 2016

Consumer Loans				
Residential First Mortgage	\$6	\$—	\$29	\$35
Home equity	1	2	11	14
Other	1	—	—	1
Total Consumer Loans	8	2	40	50
Total Loans	\$8	\$2	\$40	\$50

(1) Includes performing nonaccrual loans that are less than 90 days delinquent and for which interest cannot be accrued.

At June 30, 2017, we had \$36 million of past due (payment of principal or interest is 30 days past the scheduled payment date) LHFI. Of those past due loans, \$30 million loans were nonperforming. At December 31, 2016, we had \$50 million of past due LHFI. Of those past due loans, \$40 million loans were nonperforming. The decrease from December 31, 2016 to June 30, 2017 was primarily due to improved asset quality and the sale of nonperforming loans.

Early stage delinquencies remained low with the 30 to 59 days past due loans decreasing to \$3 million at June 30, 2017, compared to \$8 million at December 31, 2016, primarily driven by improved asset quality.

The ratio of nonperforming loans to LHFI decreased to 0.44 percent at June 30, 2017 from 0.67 percent at December 31, 2016.

Consumer loans. As of June 30, 2017, nonperforming consumer loans decreased \$10 million from December 31, 2016, primarily due to the sale of nonperforming loans and the continued improvement of our overall credit quality. Net charge-offs in consumer loans totaled less than \$1 million and \$9 million for the three months ended June 30, 2017 and June 30, 2016, respectively. Net charge-offs totaled \$4 million and \$21 million for the six months ended June 30, 2017 and June 30, 2016, respectively. Included in those amounts were charge-offs of \$1 million and \$8 million related to the sale or transfer of loans during the six months ended June 30, 2017 and June 30, 2016, respectively.

Commercial loans. As of June 30, 2017 and December 31, 2016, there were no nonperforming commercial loans. There were no net charge-offs of commercial loans for the six months ended June 30, 2017 and June 30, 2016.

Troubled debt restructurings (held-for-investment)

Troubled debt restructurings ("TDRs") are modified loans in which a borrower demonstrates financial difficulties and for which a concession has been granted as a result. The decrease of \$27 million in our total TDR loans at June 30, 2017 compared to December 31, 2016 was primarily due to the sale of nonperforming loans during the six months ended June 30, 2017. Nonperforming TDRs were 55.5 percent and 44.2 percent of total nonperforming loans at June 30, 2017 and December 31, 2016, respectively.

Nonperforming TDRs are included in nonaccrual loans. TDRs remain in nonperforming status until a borrower has made at least six consecutive months of payments under the modified terms. Performing TDRs are excluded from nonaccrual

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loans because it is reasonably assured that all contractual principal and interest due under the restructured terms will be collected. Within consumer nonperforming loans, residential first mortgage TDRs were 67.7 percent of residential first mortgage nonperforming loans at June 30, 2017, compared to 37.4 percent at December 31, 2016.

The following table sets forth a summary of TDRs by performing status and activity during each of the years presented:

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	2017	2016	2017	2016
	(Dollars in millions)			
Performing				
Beginning balance	\$48	\$74	\$67	\$101
Additions	1	2	2	7
Transfer to nonperforming TDR	(1)	(4)	(2)	(6)
Transfer from nonperforming TDR	—	4	—	5
Principal repayments	(1)	(1)	(1)	(2)
Reductions (1)	(1)	(2)	(20)	(32)
Ending balance (2)(3)	\$46	\$73	\$46	\$73
Nonperforming				
Beginning balance	\$11	\$27	\$18	\$35
Additions	1	1	2	5
Transfer from performing TDR	1	4	2	6
Transfer to performing TDR	—	(4)	—	(5)
Principal repayments	—	(1)	(1)	—
Reductions (1)	(1)	(6)	(9)	(20)
Ending balance (2)(3)	\$12	\$21	\$12	\$21

(1) Includes loans paid in full or otherwise settled, sold or charged-off.

(2) Consumer loans include residential first mortgage, home equity and other consumer loans. The ALLL on consumer TDR loans totaled \$11 million and \$12 million at June 30, 2017 and 2016.

(3) There were no commercial TDRs at June 30, 2017 and 2016.

Allowance for Loan Losses

The ALLL represents management's estimate of probable losses that are inherent in our LHFI portfolio but which have not yet been realized. The consumer loan portfolio includes residential first mortgages, home equity, and other consumer loans. The commercial loan portfolio includes CRE, C&I and warehouse lending. For further information, see Note 4 - Loans Held-for-Investment.

The ALLL as a percentage of LHFI decreased to 2.1 percent as of June 30, 2017 from 2.4 percent as of December 31, 2016. At June 30, 2017, we had a 2.5 percent allowance coverage of our consumer loan portfolio. The commercial loan ALLL coverage ratio was 1.7 percent at June 30, 2017, reflecting the continued growth in the portfolio along with the continued strong quality.

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The following tables set forth certain information regarding the allocation of our ALLL to each loan category:

June 30, 2017

	Loans Held-for- Investment Portfolio	Percent of Investment Portfolio	Allowance Amount	Allowance as a Percent of Loan Portfolio
(Dollars in millions)				
Consumer loans				
Residential first mortgage	\$2,530	37.4 %	\$ 56	2.2 %
Home equity	454	6.7 %	19	4.2 %
Other	27	0.4 %	1	3.7 %
Total consumer loans	3,011	44.5 %	76	2.5 %
Commercial loans				
Commercial real estate	1,557	23.0 %	37	2.4 %
Commercial and industrial	1,040	15.4 %	21	2.0 %
Warehouse lending	1,155	17.1 %	6	0.5 %
Total commercial loans	3,752	55.5 %	64	1.7 %
Total consumer and commercial loans (1)	\$6,763	100.0 %	\$ 140	2.1 %

(1) Excludes loans carried under the fair value option.

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2017	
	2016	2016	2016	2016
(Dollars in millions)				
Beginning balance	\$141	\$162	\$142	\$187
Provision (benefit) for loan losses	(1)	(3)	2	(16)
Charge-offs				
Consumer loans				
Residential first mortgage	(1)	(8)	(5)	(19)
Home equity	(1)	(1)	(1)	(3)
Other consumer	—	(1)	(1)	(2)
Total charge offs	(2)	(10)	(7)	(24)
Recoveries				
Consumer loans				
Residential first mortgage	1	1	1	1
Home equity	1	—	1	1
Other consumer	—	—	1	1
Total recoveries	2	1	3	3
Charge-offs, net of recoveries	—	(9)	(4)	(21)
Ending balance	\$140	\$150	\$140	\$150
Net charge-off to LHFII ratio (1)	0.04 %	0.62 %	0.15 %	0.74 %
Net charge-off ratio, adjusted (1)(2)	0.02 %	0.18 %	0.02 %	0.44 %

(1) Excludes loans carried under the fair value option.

(2) Excludes charge-offs of zero and \$2 million related to the transfer and subsequent sale of loans during the three months ended June 30, 2017 and June 30, 2016, respectively, and \$1 million and \$8 million related to the sale or transfer of loans during the six months ended June 30, 2017 and June 30, 2016, respectively. Also excludes charge-offs related to loans with government guarantees of zero and \$4 million during the three months ended June 30, 2017 and June 30, 2016, respectively, and \$2 million and \$7 million during the six months ended June 30,

2017 and June 30, 2016, respectively.

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Market Risk

Market risk is the risk of reduced earnings and or declines in the net market value of the balance sheet primarily due to changes in interest rates, currency exchange rates, or equity prices. We do not have any material foreign currency exchange risk or equity price risk. The primary market risk is interest rate risk and results from timing differences in the repricing of our assets and liabilities, changes in the relationships between rate indices, and the potential exercise of explicit or embedded options.

Interest Rate

Interest rate risk is monitored by the ALCO, which is composed of our executive officers and other members of management, in accordance with policies approved by our board of directors. In determining the appropriate level of interest rate risk, the ALCO considers the impact projected interest rate scenarios have on earnings and capital, liquidity, business strategies, and other factors. The ALCO meets monthly or as deemed necessary to review, among other things, the sensitivity of assets and liabilities to interest rate changes, the book and fair values of assets and liabilities, unrealized gains and losses, purchase and sale activity, LHFS and commitments to originate loans, and the maturities of investments, borrowings and time deposits.

Financial instruments used to manage interest rate risk include derivative financial instruments such as interest rate swaps and forward sales commitments. For further information, see Note 8 - Derivative Financial Instruments and Note 17 - Fair Value Measurements. All of our derivatives are accounted for at fair market value. All mortgage loan production originated for sale is accounted for on a fair value basis.

To effectively measure and manage interest rate risk, sensitivity analysis is used to determine the impact on earnings and the net market value of the balance sheet across various interest rate scenarios, balance sheet trends, and strategies. From these simulations, interest rate risk is quantified and appropriate strategies are developed and implemented. Additionally, duration and net interest income sensitivity measures are utilized when they provide added value to the overall interest rate risk management process. The overall interest rate risk position and strategies are reviewed by executive management and the board of directors on an ongoing basis. However, management has the latitude to increase interest rate sensitivity within certain limits if, in management's judgment, the increase will enhance profitability.

Net interest income simulation analysis provides estimated net interest income of the current balance sheet across alternative interest rate scenarios. The net interest income analysis measures the sensitivity of interest sensitive earnings over a 12 month time horizon. The analysis holds the current balance sheet values constant and does not take into account management intervention. The net interest income simulation demonstrates the level of interest rate risk inherent in the existing balance sheet.

The following table is a summary of the changes in our net interest income that are projected to result from hypothetical changes in market interest rates. The interest rate scenarios presented in the table include interest rates as of June 30, 2017 and December 31, 2016 and rates in those periods adjusted by instantaneous parallel rate changes plus or minus 200 basis points. The minus 200 basis point shock scenario is a flattener scenario as rates are floored at zero given the current interest rate levels.

June 30, 2017

Scenario	Net interest income (Dollars in millions)	\$ Change	% Change
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200	\$417	\$ 24	6.1	%
Constant	393	—	—	%
(200)	337	(56)	(14.4)	%

December 31, 2016

	Net			
Scenario	interest	\$ Change	% Change	
	income			
	(Dollars in millions)			
200	\$321	\$ 19	6.3	%
Constant	301	—	—	%
(200)	245	(57)	(18.9)	%

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At June 30, 2017, the \$92 million increase in the net interest income in the constant scenario as compared to December 31, 2016 was primarily driven by the increased size of the balance sheet.

We have also projected the potential impact to net interest income in a hypothetical interest rate scenario "bear flattener" as of June 30, 2017. When increasing short-term interest rates instantaneously by 100 basis points and holding the longer term interest rates unchanged, the decrease to net interest income over a 12-month and 24-month period based on our balance sheet as of June 30, 2017 is a loss of \$37 million and \$48 million, respectively.

In the net interest income simulation, our balance sheet exhibits slight asset sensitivity. When interest rates rise our interest income increases. Conversely when interest rates fall our interest income decreases. The net interest income simulation measures the interest rate risk of the balance sheet over a short period of time, typically 12 months. An additional analysis is completed that measures the interest rate risk over an extended period of time. The EVE analysis provides a fair value of the balance sheet in alternative interest rate scenarios. The EVE analysis does not take into account management intervention and assumes the new rate environment is constant and the change is instantaneous.

The following table is a summary of the changes in our EVE that are projected to result from hypothetical changes in market interest rates. EVE is the market value of assets, less the market value of liabilities, adjusted for the market value of off-balance sheet instruments. The interest rate scenarios presented in the table include interest rates at June 30, 2017 and December 31, 2016, and are adjusted by instantaneous parallel rate changes upward to 300 basis points and downward to 100 basis points. The scenarios are not comparable due to differences in the interest rate environments, including the absolute level of rates and the shape of the yield curve. Each rate scenario reflects unique prepayment, repricing, and reinvestment assumptions. Management derives these assumptions by considering published market prepayment expectations, the repricing characteristics of individual instruments or groups of similar instruments, our historical experience, and our asset and liability management strategy. Further, this analysis assumes that certain instruments would not be affected by the changes in interest rates or would be partially affected due to the characteristics of the instruments.

Further, as this framework evaluates risks to the current statement of financial condition only, changes to the volumes and pricing of new business opportunities that can be expected in the different interest rate outcomes are not incorporated in this analytical framework. For instance, analysis of our history suggests that declining interest rate levels are associated with higher loan production volumes at higher levels of profitability. While this "natural business hedge" historically offsets most, if not all, of the identified risks associated with declining interest rate scenarios, these factors fall outside of the EVE framework. Further, there can be no assurance that this natural business hedge would positively affect the EVE in the same manner and to the same extent as in the past.

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

If EVE increases in any interest rate scenario, that would indicate an increasing direction for the margin in that hypothetical rate scenario. A perfectly matched balance sheet would possess no change in the EVE, no matter what the rate scenario. The following table presents the EVE in the stated interest rate scenarios:

June 30, 2017					December 31, 2016				
Scenario	EVE	EVE%	\$ Change	% Change	Scenario	EVE	EVE%	\$ Change	% Change
	(Dollars in millions)					(Dollars in millions)			
300	\$2,391	14.8 %	\$ (129)	(5.1)%	300	\$1,927	13.9 %	\$ (173)	(8.2)%
200	2,456	15.2 %	(63)	(2.5)%	200	2,005	14.4 %	(95)	(4.5)%
100	2,511	15.6 %	(9)	(0.4)%	100	2,073	14.9 %	(28)	(1.3)%

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Current	2,519	15.6 %	—	—	%	Current	2,100	15.1 %	—	—	%
(100)	2,472	15.3 %	(47)	(1.9)%	(100)	2,067	14.9 %	(33)	(1.6)%

Our balance sheet exhibits sensitivity in a rising interest rate scenario as the EVE decreases. The decrease in EVE is the result of the amount of liabilities that would be expected to reprice exceeding the amount of assets repriced in the up 200 scenario. The December 31, 2016 (100) is a flattener scenario as shorter term rates are unable to decrease 100 basis points due to the absolute level of rates. Therefore, the yields of the longer term variable rate assets decrease by the full 100 basis points, but the liabilities repricing to shorter term rates decrease to less than 100 basis points, leading to a reduction in EVE.

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Mortgage Market Risk

We utilize multiple production channels to originate or acquire mortgage loans on a national scale to generate high returns on equity capital. This helps grow the servicing business and provides stable, low cost funding for the Community Bank segment. We continue to leverage technology to streamline the mortgage origination process, thereby bringing service and convenience to borrowers and correspondents. We also continue to make available to our customers various web-based tools that facilitate the mortgage loan process through each of our production channels. We will continue to seek new ways to expand our relationships with borrowers and correspondents to provide the necessary capital and liquidity to grow Mortgage Servicing and the Community Bank segment.

We are a leading national originator of mortgage loans based on our residential first mortgage loan originations. The following table discloses residential first mortgage loan originations by channel, type and mix for each respective period:

	Three Months		Six Months	
	Ended June 30,		Ended June 30,	
	2017	2016	2017	2016
	(Dollars in millions)			
Correspondent	\$6,993	\$6,200	\$11,448	\$10,961
Broker	1,438	1,625	2,479	2,895
Retail	753	496	1,160	808
Total	\$9,184	\$8,321	\$15,087	\$14,664
Purchase originations	\$5,458	\$3,837	\$8,515	\$6,525
Refinance originations	3,726	4,484	6,572	8,139
Total	\$9,184	\$8,321	\$15,087	\$14,664
Conventional	\$4,601	\$4,763	\$7,560	\$8,562
Government	2,431	2,060	4,121	3,585
Jumbo	2,152	1,498	3,406	2,517
Total	\$9,184	\$8,321	\$15,087	\$14,664

Correspondent. In the correspondent channels, an unaffiliated bank or mortgage company completes the loan paperwork and also funds the loan at closing. After the bank or mortgage company has funded the transaction, we purchase the loan at an agreed upon price. We perform a full review of each loan, whether purchased in bulk or not, purchasing only those loans that were originated in accordance with our underwriting guidelines. Correspondents apply to the Bank and may be approved for delegated underwriting authority. Delegated correspondents assume the risks associated with the underwriting of the loan and earn more on loans sold compared to non-delegated correspondents. Non-delegated correspondents earn commissions and administrative fees for closing and funding loans which are then underwritten by the Bank. We have active correspondent relationships with 1,014 companies located in all 50 states, ranking us as the sixth largest correspondent lender.

Broker. In a broker transaction, an unaffiliated mortgage broker completes several steps of the loan origination process including the loan paperwork, but the loans are underwritten by us on a loan-level basis to our underwriting standards and we fund and close the loan in the Bank's name, thereby becoming the lender of record. We rank eighth largest in total broker originations with 689 active mortgage broker relationships located in all 50 states.

Retail. In our retail channel, loans are originated through our nationwide network of stand-alone home loan centers. At June 30, 2017, we maintained 85 retail locations in 26 states with the Opes acquisition adding 39 locations in 3 states at the time of acquisition. In a direct-to-consumer lending transaction, loans are originated through our Community Bank segment banking centers, our Opes division and from a national direct-to-consumer call center, all of which may leverage our existing customer relationships. When loans are originated on a retail basis, most aspects of the lending

process are completed internally, including the origination documentation (inclusive of customer disclosures), as well as the funding of the transactions. Our centralized loan processing provides efficiencies and allows lending sales staff to focus on business development.

The majority of our total loan originations during the six months ended June 30, 2017 represented mortgage loans that were collateralized by residential first mortgages on single-family residences and were eligible for sale to the Agencies. In addition, we originate or purchase residential first mortgage loans, other consumer loans, and commercial loans for our LHFI portfolios. Our revenues include noninterest income from sales of residential first mortgages to the Agencies, net interest income, and revenue from servicing of loans for others.

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Our Mortgage Origination segment provides us with a large number of customer relationships through our servicing of loans sold to the Agencies and those loans we retain. These relationships, along with our banking customer relationships, provide us an opportunity to cross-sell a full line of consumer financial products which include mortgage refinancing, home equity, and other consumer loans.

We primarily utilize borrowings from the FHLB to fund our mortgage LHFS and our warehouse lending portfolio. The FHLB provides funding on a fully collateralized basis to us. Our borrowing capacity with the FHLB is a function of the amount of eligible collateral pledged, which includes residential first mortgage loans, home equity lines of credit, and commercial real estate loans.

Mortgage Servicing

We are a top 10 national mortgage servicer. The Mortgage Servicing segment services and subservices mortgage loans for others on a fee for service basis and may also collect ancillary fees and earn income through the use of noninterest-bearing escrows. Revenue for those serviced and subserved loans is earned on a contractual fee basis, with the fees varying based on our responsibilities and the status of the underlying loans. The Mortgage Servicing segment provides servicing of residential mortgages for our own LHFI portfolio in the Community Banking segment for which it earns revenue via an intercompany service fee allocation.

For further information, see Note 7 - Mortgage Servicing Rights.

The following table presents the unpaid principal balance (net of write downs) of residential loans serviced and subserved and the number of accounts associated with those loans.

	June 30, 2017		December 31, 2016	
	Amount	Number of accounts	Amount	Number of accounts
	(Dollars in millions)			
Residential loan servicing				
Serviced for own loan portfolio (1)	\$7,156	30,875	\$5,816	29,244
Serviced for others	16,144	66,106	31,207	133,270
Subserved for others (2)	63,991	304,830	43,127	220,075
Total residential loans serviced	\$87,291	401,811	\$80,150	382,589

(1) Includes LHFI (residential first mortgage and home equity), LHFS (residential first mortgage), loans with government guarantees (residential first mortgage), and repossessed assets.

(2) Includes temporary short-term subservicing performed as a result of sales of servicing-released MSRs. Includes repossessed assets.

Liquidity Risk

Liquidity risk is the risk that we will not have sufficient funds to meet current and future cash flow needs as they become due. The liquidity of a financial institution reflects our ability to meet loan requests, to accommodate possible outflows in deposits and to take advantage of interest rate and market opportunities. The ability of a financial institution to meet current financial obligations is a function of the balance sheet structure, the ability to liquidate assets, and access to various sources of funds.

We primarily originate agency-eligible LHFS and therefore the majority of new residential first mortgage loan originations are readily convertible to cash, either by selling them as part of our monthly agency sales, private party whole loan sales, or by pledging them to the FHLB of Indianapolis and borrowing against them. We use the FHLB of Indianapolis as a significant source for funding our residential mortgage banking business due to the flexibility in terms of being able to borrow or repay borrowings as daily cash needs require.

We have arrangements with the FRB of Chicago to borrow as appropriate from its discount window. The discount window is also a borrowing facility that is intended to be used only for short-term liquidity needs arising from special or unusual circumstances. The amount we are allowed to borrow is based on the lendable value of the collateral that we provide. To collateralize the line, we pledge investment securities and loans that are eligible based on FRB of Chicago guidelines. At June 30, 2017 and December 31, 2016, we had no borrowings outstanding against this line of credit.

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The amount we can borrow, or the value we receive for the assets pledged to our liquidity providers, varies based on the amount and type of pledged collateral as well as the perceived market value of the assets and the "haircut" of the market value of the assets. That value is sensitive to the pricing and policies of our liquidity providers and can change with little or no notice.

Our Consolidated Statements of Cash Flows shows cash used in operating activities of \$12.0 billion and \$5.2 billion for the six months ended June 30, 2017 and 2016, respectively. This primarily reflects our mortgage operations and is a reflection of the manner in which we execute certain loan sales for which the cash outflow is considered an operating activity and the corresponding cash inflow is considered an investing activity. For the period ending June 30, 2017, operating cash flows declined primarily due to our election to extend the amount of time we hold mortgage-backed securities related to our LHFS portfolio.

As governed and defined by our internal liquidity policy, we maintain adequate excess liquidity levels appropriate to cover unanticipated liquidity needs. In addition to this liquidity, we also maintain targeted minimum levels of unused collateralized borrowing capacity as another cushion against unexpected liquidity needs. Each business day, we forecast 90 days of daily cash needs. This allows us to determine our projected near term daily cash fluctuations and also to plan and adjust, if necessary, future activities. As a result, in an adverse environment, we would be able to make adjustments to operations as required to meet the liquidity needs of our business, including adjusting deposit rates to increase deposits, planning for additional FHLB borrowings, accelerating sales of LHFS (agencies and/or private), selling LHFI or investment securities, borrowing through the use of repurchase agreements, reducing originations, making changes to warehouse funding facilities, or borrowing from the discount window.

Our liquidity position is continuously monitored and adjustments are made to the balance between sources and uses of funds as deemed appropriate. We balance the liquidity of our loan assets to our available funding sources. Our LHFI portfolio is funded with stable core deposits whereas our warehouse and LHFS may be funded with FHLB borrowings.

Management is not aware of any events that are reasonably likely to have a material adverse effect on our liquidity, capital resources or operations.

Parent Company Liquidity

The Company obtains its liquidity from multiple sources, including dividends from the Bank and the issuance of debt and equity securities. The primary uses of the Company's liquidity are debt service and operating expenses. At June 30, 2017 the Company held \$128 million of cash at the Bank, or 3.3 years of expense and debt service coverage.

The OCC regulates all capital distributions made by the Bank, directly or indirectly, to the holding company, including dividend payments. A subsidiary of a savings and loan holding company, such as the Bank, must file a notice or application with the OCC at least 30 days prior to each proposed capital distribution. Whether an application is required is based on a number of factors including whether the institution qualifies for expedited treatment under the OCC rules and regulations or if the total amount of all capital distributions (including each proposed capital distribution) for the applicable calendar year exceeds net income for that year to date plus the retained net income for the preceding two years. In addition, as a subsidiary of a savings and loan holding company, the Bank must receive approval from the FRB before declaring any dividends. Additional restrictions on dividends apply if the Bank fails the QTL test.

For further information and restrictions related to the Bank's payment of dividends, see MD&A - Capital and Regulatory Risk.

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Bank Liquidity

	June 30,	December 31,	Change
	2017	2016	
	(Dollars in millions)		
Demand deposit accounts	\$1,230	\$ 1,134	\$96
Savings accounts	3,916	3,887	29
Money market demand accounts	248	247	1
Certificates of deposit/CDARS	1,153	1,056	97
Total retail deposits	6,547	6,324	223
Government deposits	851	1,030	(179)
Company controlled deposits	1,297	1,446	(149)
Total deposits	\$8,695	\$ 8,800	\$(105)
Federal Home Loan Bank advances	\$4,870	\$ 2,980	\$1,890
Other long-term debt	493	493	—
Total borrowed funds	\$5,363	\$ 3,473	\$1,890

Deposits

We continue to focus on increasing our core deposits which includes demand deposits, savings, and money market accounts that provides a lower cost funding source to the Bank. During the six months ended June 30, 2017, our core deposits increased \$126 million primarily driven by direct mailing advertising and an increase in commercial demand deposits.

We utilize local governmental agencies, and other public units, as an additional source for deposit funding. As a Michigan bank, we are not required to hold collateral against our government deposits from Michigan municipalities as they are covered by the Michigan Business and Growth Fund. This results in higher margins earned on these deposits which can be used to fund higher yielding commercial loans. Government deposit accounts include \$286 million of certificates of deposit with maturities typically less than one year and \$565 million in checking and savings accounts at June 30, 2017.

Company controlled deposits arise due to our servicing or sub-servicing of loans for others and represent the portion of the investor custodial accounts on deposit with the Bank. Certain deposits require us to reimburse the owner for the spread on these funds. This cost is a component of net loan administration income. During the six months ended June 30, 2017, these deposits decreased \$149 million, primarily due to a decrease in taxes and insurance balances.

We participate in the CDARS program, through which certain customer CDs are exchanged for CDs of similar amounts from other participating banks. This gives customers the potential to receive FDIC insurance up to \$50 million. At June 30, 2017, we had \$208 million of total CDs enrolled in the CDARS program. The total CDARS balances decreased \$23 million at June 30, 2017 from December 31, 2016.

FHLB Advances

We rely upon advances from the FHLB as a source of funding for the origination or purchase of loans for sale in the secondary market and for providing duration specific short-term and long-term financing. The outstanding balance of FHLB advances fluctuates from time to time depending on our current inventory of mortgage LHFS and the availability of lower cost funding sources. Our portfolio includes short-term fixed rate advances, long-term LIBOR adjustable advances, and long-term fixed rate advances. Interest rates on the LIBOR index advances reset every three months and the advances may be prepaid without penalty, with notification, at scheduled three-month intervals after an initial 12-month lockout period.

The FHLB provides loans, also referred to as advances, on a fully collateralized basis, to savings banks and other member financial institutions. We are currently authorized through a resolution of our board of directors to apply for advances from the FHLB using approved loan types as collateral. At June 30, 2017, we had the authority and approval from the FHLB to utilize a line of credit of up to \$7.0 billion and we may access that line to the extent that collateral is provided. At June 30, 2017, we had \$4.9 billion of advances outstanding and an additional \$798 million of collateralized borrowing capacity available at the FHLB. At June 30, 2017, we pledged collateral to the Federal Reserve Discount Window amounting to \$461 million with a lendable value of \$445 million. At December 31, 2016, we pledged collateral to the Federal Reserve Discount Window amounting to \$496 million with a lendable value of \$474 million. At June 30, 2017 and December 31, 2016, we had

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no borrowings outstanding against this line of credit.

Debt

As part of our overall capital strategy, we previously raised capital through the issuance of junior subordinated notes to our special purpose trusts formed for the offerings, which issued Tier 1 qualifying preferred stock (trust preferred securities). The trust preferred securities are callable by us at any time. Interest is payable on a quarterly basis; however, we may defer interest payments for up to 20 quarters without default or penalty. At June 30, 2017, we had no deferred interest payments.

On July 11, 2016, we issued \$250 million of 2021 Senior Notes which mature on July 15, 2021. The proceeds from these notes were used to bring current and redeem our outstanding Series C Preferred Stock.

Prior to June 15, 2021, we may redeem some or all of the 2021 Senior Notes at a redemption price equal to the greater of 100 percent of the aggregate principal amount of the 2021 Senior Notes to be redeemed or the sum of the present values of the remaining scheduled payments plus, in each case, accrued and unpaid interest.

For further information, see Note 9 - Borrowings.

Operational Risk

Operational risk is the risk of loss due to human error; inadequate or failed internal systems and controls; violations of, or noncompliance with, laws, rules and regulations, prescribed practices, or ethical standards; and external influences such as market conditions, fraudulent activities, disasters, and security risks. We continuously strive to strengthen our system of internal controls to ensure compliance with laws, rules, and regulations, and to improve the oversight of our operational risk.

We evaluate internal systems, processes, and controls to mitigate loss from cyber-attacks and, to date, have not experienced any material losses. The goal of this framework is to implement effective operational risk techniques and strategies, minimize operational and fraud losses, and enhance our overall performance.

Loans with government guarantees

Substantially all of our loans with government guarantees continue to be insured or guaranteed by the FHA or the U.S. Department of Veterans Affairs and management believes that the reimbursement process is proceeding appropriately. Nonperforming repurchased loans in this portfolio earn interest at a rate based upon the 10-year U.S. Treasury note rate from the time the underlying loan becomes delinquent, which is not paid by the FHA until claimed. Certain loans within our portfolio may be subject to indemnifications and insurance limits which exposes us to limited credit risk. In the three and six months ended June 30, 2017, we experienced net charge-offs of less than \$1 million and \$2 million, respectively, and have reserved for the remaining risks within other assets and as a component of our ALLL on residential first mortgages. These charge-offs arise due to insurance limits on VA insured loans and FHA property foreclosure and preservation requirements that may result in a loss of the guarantee.

For further information, see Note 5 - Loans with Government Guarantees.

Representation and warranty reserve

When we sell mortgage loans, we make customary representations and warranties to the purchasers, including sponsored securitization trusts and their insurers (primarily Fannie Mae and Freddie Mac).

The representation and warranty benefit of \$3 million and \$7 million during the three and six months ended June 30, 2017, respectively, was primarily due to ongoing refinements in our assumptions to reflect repurchase experience related to recent vintages along with reduction in reserve estimates associated with indemnification agreements with the U.S. Department of Housing and Urban Development.

During the six months ended June 30, 2017, we had \$9 million in Fannie Mae new repurchase demands and \$5 million in Freddie Mac new repurchase demands. These amounts are down as compared to the six months ended June 30, 2016 when we had \$11 million in Fannie Mae new repurchase demands and \$9 million in Freddie Mac new repurchase demands. The total UPB of 2009 and later vintage loans, which are subject to the representation and warranty reserve, sold to Fannie Mae and Freddie Mac was \$191 million and \$172 million at June 30, 2017 and June 30, 2016, respectively.

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For further information on Representation and Warranty Reserve, see Note 10 - Representation and Warranty Reserve.

Regulatory Risks

Consent Orders

On September 29, 2014, the Bank entered into a Consent Order with the CFPB. The Consent Order relates to alleged violations of federal consumer financial laws arising from the Bank's residential first mortgage loan loss mitigation practices and default servicing operations dating back to 2011. Under the terms of the Consent Order, the Bank paid \$28 million for borrower remediation and \$10 million in civil money penalties. The settlement does not involve any admission of wrongdoing on the part of the Bank or our employees, directors, officers, or agents. For further information and a complete description of all of the terms of the Consent Order, please refer to our Current Report on Form 8-K filed on September 29, 2014.

Supervisory Agreement

On January 28, 2010, we became subject to the Supervisory Agreement, which will remain in effect until terminated, modified, or suspended in writing by the Federal Reserve. The failure to comply with the Supervisory Agreement could result in the initiation of further enforcement action by the Federal Reserve, including the imposition of further operating restrictions, and could result in additional enforcement actions against us. We have taken actions which we believe are appropriate to comply with, and intend to maintain compliance with, all of the requirements of the Supervisory Agreement. For further information and a complete description of all of the terms of the Supervisory Agreement, please refer to the copy of the Supervisory Agreement filed with the SEC as an exhibit to our 2016 Form 10-K filed on March 13, 2017.

Department of Justice Settlement Agreement

On February 24, 2012, the Bank entered into a Settlement Agreement with the DOJ under which we made an initial payment of \$15 million and agreed to make future payments totaling \$118 million in annual increments of up to \$25 million upon meeting all of the following conditions which are evaluated quarterly and include: (a) the reversal of the DTA valuation allowance, which occurred at the end of 2013; (b) the repayment of the Fixed Rate Cumulative Perpetual Preferred Stock, Series C (the "TARP Preferred"), which occurred in July 2016; and (c) the Bank having a Tier 1 Leverage Capital Ratio of 11 percent or greater as filed in the Call Report with the OCC.

No payment would be required until six months after the Bank files its Call Report first reporting that its Tier 1 Leverage Capital Ratio was 11 percent or greater. If all other conditions were then satisfied, an initial annual payment of \$25 million would be due at that time. The next annual payment is only made if all conditions continue to be satisfied otherwise payments are delayed until all such conditions are met. Further, making such a payment must not violate any material banking regulatory requirement, and the OCC must not object in writing.

The combination of (a) future dividends from the Bank to Bancorp and (b) continued growth in earning assets at the Bank are expected to continue to limit the growth rate of the Bank's Tier 1 Leverage Capital Ratio, which could have an impact on the timing of expected cash flows under the Settlement Agreement.

Consistent with our business and regulatory requirements, Flagstar shall seek in good faith to fulfill the conditions, and will not undertake any conduct or fail to take any action the purpose of which is to frustrate or delay our ability to fulfill any of the conditions.

Additionally, if the Bank or Bancorp become party to a business combination in which the Bank and Bancorp represent less than 33.3 percent of the resulting company's assets, annual payments would commence twelve months

after the date of that business combination.

The Settlement Agreement meets the definition of a financial instrument for which we elected the fair value option. The fair value of the liability is subject to significant uncertainty and is impacted by forecasted estimates of equity, earnings, timing and amount of dividends and growth of the balance sheet and their related impacts on forecasted Tier 1 Leverage Capital Ratio. We consider the assumptions a market participant would make to transfer the liability and evaluate multiple possible outcomes and our estimates of the likelihood of these outcomes, which may change over time.

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Capital Risk

Under the OCC's capital distribution regulations, a savings bank that is a subsidiary of a savings and loan holding company must either notify or seek approval from the OCC of a capital distribution at least 30 days prior to the declaration of a dividend or the approval by the board of directors of the proposed capital distribution. The 30-day period allows the OCC to determine whether the distribution would not be advisable. Also, under Federal Reserve requirements, the Bank must provide a 30-day notice to the Federal Reserve prior to declaring or paying dividends. In addition, under the Supervisory Agreement, the Company agreed to request prior non-objection of the Federal Reserve to pay dividends or other capital distributions. We seek to manage our capital levels and overall business in a manner which we consider to be prudent and work with our regulators to ensure that our capital levels are appropriate considering our risk profile and evaluation of the capital levels maintained by peer institutions.

In the second quarter 2017, we paid dividends of \$24 million from the Bank to the Bancorp. To support the on-going debt service and other Bancorp expenses, we also intend to reduce our Bancorp double leverage and debt to equity ratios to be more consistent with such ratios at other mid-sized banks, which would likely require further dividend payments from the Bank to the Bancorp for the foreseeable future.

Regulatory Capital Composition - Transition

The maintenance of appropriate levels of capital is monitored by management on a regular basis. We manage our funding and capital positions by making adjustments to our balance sheet size and composition and hold capital to protect liability holders from the risk of loss.

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

Effective January 1, 2015, we became subject to the Basel III rules, which include certain transition provisions. Capital deductions to the Company's MSRs and deferred tax assets are recognized in 20 percent annual increments, and will be fully recognized as of January 1, 2018. When presented on a fully phased-in basis, capital, risk-weighted assets, and the capital ratios assume all regulatory capital adjustments and deductions are fully recognized. At June 30, 2017, the Company and the Bank were subject to the transitional phase-in limitation on deductions related to MSRs and certain deferred tax assets. The annual incremental change in the deductions due to the increase in the transitional phase-in from 60 percent in 2016 to 80 percent in 2017 reduced our regulatory capital ratios. These transitional phase in amounts increase to 100 percent in 2018.

Effective January 1, 2016, we became subject to the capital conservation buffer under the Basel III rules, subjecting a banking organization to certain limitations on capital distributions and discretionary bonus payments to executive officers if the organization does not maintain a capital conservation buffer above the minimum risk based capital requirements. The capital conservation buffer for 2017 must be greater than 1.25 percent in order to not be subject to limitations. The Company and the Bank had a capital conservation buffer of 7.9 percent and 9.7 percent, respectively, as of June 30, 2017. When fully phased-in on January 1, 2019, the capital conservation buffer must be greater than 2.5 percent.

Dodd-Frank Act Section 171, commonly known as the Collins Amendment, grandfathered the regulatory capital treatment of hybrid securities, such as trust preferred securities issued prior to May 9, 2010, for banks or holding

companies with less than \$15 billion in total consolidated assets as of December 31, 2009.

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At June 30, 2017, we were considered "well-capitalized" for regulatory purposes. The following tables show the regulatory capital ratios as of the dates indicated:

	June 30, 2017		December 31, 2016	
	Amount	Ratio	Amount	Ratio
	(Dollars in millions)			
Bancorp				
Tier 1 leverage (to adjusted avg. total assets)	\$1,408	9.10 %	\$1,256	8.88 %
Total adjusted avg. total asset base (1)	15,468		14,149	
Tier 1 capital (to RWA)	\$1,408	14.65 %	\$1,256	15.12 %
Common equity Tier 1 (to RWA)	1,196	12.45 %	1,084	13.06 %
Total capital (to RWA)	1,530	15.92 %	1,363	16.41 %
Risk-weighted asset base (1)	\$9,610		\$8,305	

	June 30, 2017		December 31, 2016	
	Amount	Ratio	Amount	Ratio
	(Dollars in millions)			
Bank				
Tier 1 leverage (to adjusted avg. total assets)	\$1,590	10.26 %	\$1,491	10.52 %
Total adjusted avg. total asset base (1)	15,504		14,177	
Tier 1 capital (to RWA)	\$1,590	16.49 %	\$1,491	17.90 %
Common equity Tier 1 (to RWA)	1,590	16.49 %	1,491	17.90 %
Total capital (to RWA)	1,712	17.75 %	1,598	19.18 %
Risk-weighted asset base (1)	\$9,645		\$8,332	

(1) Based on adjusted total assets for purposes of Tier 1 leverage capital and RWA for purposes Tier 1, common equity Tier 1, and total risk-based capital.

Our Bancorp Tier 1 leverage ratio increased at June 30, 2017, compared to December 31, 2016, primarily as a result of MSR sales and earnings, offset by an increase in the deductions related to DTAs and MSRs due to the change in transitional phase-in limitation from 60 percent at December 31, 2016 to 80 percent at June 30, 2017.

Banks with assets greater than \$10 billion are required to submit a DFAST under the final rules established by their primary regulator. DFAST requires banks to project results over a nine-quarter planning horizon under three scenarios (baseline, adverse, and severely adverse) published by the Federal Reserve and to show that the bank would exceed regulatory minimum capital standards for the Tier 1 leverage ratio, Tier 1 common ratio, Tier 1 risk-based capital ratio, and the Total risk-based capital ratio under all of these scenarios. We are not subject to the Federal Reserve's Comprehensive Capital Analysis and Review program.

Certain regulatory capital ratios for the Bank and the Company are shown in the following table:

	Regulatory Minimums		Regulatory Minimums to be Well-Capitalized		Bank	Bancorp
June 30, 2017						
Basel III Ratios (transitional)						
Common equity Tier I capital ratio	4.50	%	6.50	%	16.49%	12.45 %
Tier I leverage ratio	4.00	%	5.00	%	10.26%	9.10 %
Basel III Ratios (fully phased-in) (1)						
Common equity Tier I capital ratio	4.50	%	6.50	%	15.71%	11.42 %
Tier I leverage ratio	4.00	%	5.00	%	10.13%	8.83 %

(1) Refer to MD&A - Use of Non-GAAP Financial Measures.

The impact under the fully phased in Basel III rules to our Tier 1 leverage ratio is mostly driven by the treatment that MSR's receive under Basel III. Once fully phased in, the Basel III capital rules will significantly reduce the allowable amount of the fair value of MSR's included in Tier 1 capital. At June 30, 2017, we had \$184 million of MSR's, representing 13.1 percent of

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Tier 1 capital. Our ratio of MSRs to Tier 1 capital was 26.7 percent at December 31, 2016. In the first half of 2017, we have had \$256 million in bulk MSR sales. Over the long term, we plan to continue to reduce our MSRs to Tier 1 ratio, taking into consideration market conditions to guide our pace of MSR reduction.

Use of Non-GAAP Financial Measures

In addition to results presented in accordance with GAAP, this report includes non-GAAP financial measures such as the estimated fully implemented Basel III capital levels and ratios and tangible book value per share. We believe these non-GAAP financial measures provide additional information that is useful to investors in helping to understand the underlying performance and trends of the Company.

Non-GAAP financial measures have inherent limitations, which are not required to be uniformly applied and are not audited. Readers should be aware of these limitations and should be cautious with respect to the use of such measures. To mitigate these limitations, we have practices in place to ensure that these measures are calculated using the appropriate GAAP or regulatory components in their entirety and to ensure that our performance is properly reflected to facilitate consistent period-to-period comparisons. Our method of calculating these non-GAAP measures may differ from methods used by other companies. Although we believe the non-GAAP financial measures disclosed in this report enhance investors' understanding of our business and performance, these non-GAAP measures should not be considered in isolation, or as a substitute for those financial measures prepared in accordance with GAAP. Where non-GAAP financial measures are used, the most directly comparable GAAP or regulatory financial measure, as well as the reconciliation to the most directly comparable GAAP or regulatory financial measure, can be found in this report.

Nonperforming assets / Tier 1 + Allowance for Loan Losses. The ratio of nonperforming assets to Tier 1 and ALLL divides the total level of nonperforming LHFI assets by Tier 1 capital (to adjusted total assets), as defined by bank regulations, plus ALLL. We believe these measurements are meaningful measures of capital adequacy used by investors, regulators, management and others to evaluate the adequacy of capital in comparison to other companies within the industry.

	June 30, 2017	March 31, 2017	December 31, 2016	September 30, 2016	June 30, 2016
	(Dollars in millions)				
Nonperforming assets / Tier 1 capital + ALLL					
Nonperforming assets	\$39	\$41	\$ 54	\$ 55	\$63
Tier 1 capital (to adjusted total assets)	1,408	1,277	1,256	1,225	1,514
Allowance for loan losses	140	141	142	143	150
Tier 1 capital + ALLL	\$1,548	\$1,418	\$ 1,398	\$ 1,368	\$1,664
Nonperforming assets / Tier 1 capital + ALLL	2.5	% 2.9	% 3.9	% 4.0	% 3.8

Tangible book value per share. The Company believes that tangible book value per share provides a meaningful representation of its operating performance on an ongoing basis. Management uses this measure to assess performance of the Company against its peers and evaluate overall performance. The Company believes this non-GAAP financial measure provides useful information for investors, securities analysts and others because it provides a tool to evaluate the Company's performance on an ongoing basis and compared to its peers.

	June 30, 2017	December 31, 2016	June 30, 2016
	(Dollars in millions, except share data)		
Total stock holders' equity	\$1,408	\$ 1,336	\$ 1,599

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Preferred stock	—	—	267
Goodwill and intangibles	20	—	—
Tangible book value	\$1,388	\$ 1,336	\$ 1,332
Number of common shares outstanding	57,161,456	56,824,802	56,575,779
Tangible book value per share	\$24.29	\$ 23.50	\$ 23.54

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Basel III (transitional) to Basel III (fully phased-in) reconciliation. On January 1, 2015, the Basel III rules became effective, subject to transition provisions primarily related to regulatory deductions and adjustments impacting common equity Tier 1 capital and Tier 1 capital. When fully phased-in, Basel III, will increase capital requirements through higher minimum capital levels as well as through increases in risk-weights for certain exposures. Additionally, the final Basel III rules place greater emphasis on common equity. In October 2013, the OCC and Federal Reserve released final rules detailing the U.S. implementation of Basel III and the application of the risk-based and leverage capital rules to top-tier savings and loan holding companies. We have transitioned to the Basel III framework beginning in January 2015 and are subject to a phase-in period extending through 2018. Accordingly, the calculations provided below and on the previous page, are estimates. These measures are considered to be non-GAAP financial measures because they are not formally defined by GAAP and the Basel III implementation regulations. The Common Equity Tier 1, Tier 1, Total Capital and Leverage ratios will not be fully phased-in until January 1, 2018 and the Capital Conservation buffer will not be fully phased-in until January 1, 2019. The regulations are subject to change as clarifying guidance becomes available and the calculations currently include our interpretations of the requirements including informal feedback received through the regulatory process. Other entities may calculate the Basel III ratios differently from ours based on their interpretation of the guidelines. Since analysts and banking regulators may assess our capital adequacy using the Basel III framework, we believe that it is useful to provide investors information enabling them to assess our capital adequacy on the same basis.

	Common Equity Tier 1 Tier 1 (to Risk Weighted Assets) (Dollars in millions)	Tier 1 leverage (to adjusted avg. total assets)	Tier 1 Capital (to Risk Weighted Assets)	Total Risk-Based Capital (to Risk Weighted Assets)	
June 30, 2017					
Flagstar Bancorp					
Regulatory capital – Basel III (transitional) to Basel III (fully phased-in)					
Basel III (transitional)	\$1,196	\$1,408	\$1,408	\$1,530	
Increased deductions related to deferred tax assets, MSRs, and other capital components	(75)	(47)	(47)	(44)	
Basel III (fully phased-in) capital	\$1,121	\$1,361	\$1,361	\$1,486	
Risk-weighted assets – Basel III (transitional) to Basel III (fully phased-in)					
Basel III assets (transitional)	\$9,610	\$15,468	\$9,610	\$9,610	
Net change in assets	206	(46)	206	206	
Basel III (fully phased-in) assets	\$9,816	\$15,422	\$9,816	\$9,816	
Capital ratios					
Basel III (transitional)	12.45 %	9.10 %	14.65 %	15.92 %	
Basel III (fully phased-in)	11.42 %	8.83 %	13.87 %	15.14 %	
	Common Equity Tier 1 Tier 1 (to Risk Weighted Assets) (Dollars in millions)	Tier 1 leverage (to adjusted avg. total assets)	Tier 1 Capital (to Risk Weighted Assets)	Total Risk-Based Capital (to Risk-Weighted Assets)	
June 30, 2017					
Flagstar Bank					

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Regulatory capital – Basel III (transitional) to Basel III (fully phased-in)					
Basel III (transitional)	\$1,590	\$1,590	\$1,590	\$1,712	
Increased deductions related to deferred tax assets, MSRs, and other capital components	(22)	(22)	(22)	(19)	
Basel III (fully phased-in) capital	\$1,568	\$1,568	\$1,568	\$1,693	
Risk-weighted assets – Basel III (transitional) to Basel III (fully phased-in)					
Basel III assets (transitional)	\$9,645	\$15,504	\$9,645	\$9,645	
Net change in assets	331	(23)	331	331	
Basel III (fully phased-in) assets	\$9,976	\$15,481	\$9,976	\$9,976	
Capital ratios					
Basel III (transitional)	16.49 %	10.26 %	16.49 %	17.75 %	
Basel III (fully phased-in)	15.71 %	10.13 %	15.71 %	16.97 %	

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Critical Accounting Estimates

Various elements of our accounting policies, by their nature, are subject to estimation techniques, valuation assumptions and other subjective assessments. Certain accounting policies that, due to the judgment, estimates and assumptions in those policies are critical to an understanding of our Consolidated Financial Statements, in Item 1. Financial Statements herein. These policies relate to: (a) the determination of our ALLL; and (b) fair value measurements. We believe the judgment, estimates and assumptions used in the preparation of our Consolidated Financial Statements and the Notes, in Item 1, are appropriate given the factual circumstances at the time. However, given the sensitivity of our Consolidated Financial Statements and the Notes, in Item 1, herein, to these critical accounting policies, the use of other judgments, estimates and assumptions could result in material differences in our results of operations and/or financial condition. For further information on our critical accounting policies, please refer to our Annual Report on Form 10-K for the year ended December 31, 2016, which is available on our website, flagstar.com, under the Investor Relations section, or on the website of the Securities and Exchange Commission, at sec.gov.

FORWARD – LOOKING STATEMENTS

Certain statements in this Form 10-Q, including but not limited to statements included within the Management's Discussion and Analysis of Financial Condition and Results of Operations, are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. In addition, Flagstar Bancorp, Inc. may make forward-looking statements in our other documents filed with or furnished to the SEC, and our management may make forward-looking statements orally to analysts, investors, representatives of the media and others.

Generally, forward-looking statements are not based on historical facts but instead represent management's beliefs regarding future events. Such statements may be identified by words such as believe, expect, anticipate, intend, plan, estimate, may increase, may fluctuate, and similar expressions or future or conditional verbs such as will, should, would and could. Such statements are based on management's current expectations and are subject to risks, uncertainties and changes in circumstances. Actual results and capital and other financial conditions may differ materially from those included in these statements due to a variety of factors, including without limitation the precautionary statements included within each individual business' discussion and analysis of our results of operations and the risk factors listed and described in Item 1A to Part I of our Annual Report on Form 10-K for the year ended December 31, 2016 and Item 1A to Part II of this Quarterly Report on Form 10-Q, which are incorporated by reference herein, for further information on these and other factors affecting us.

Other than as required under United States securities laws, Flagstar Bancorp does not undertake to update the forward-looking statements to reflect the impact of circumstances or events that may arise after the date of the forward-looking statements.

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Item 1. Financial Statements

Flagstar Bancorp, Inc.

Consolidated Statements of Financial Condition

(In millions, except share data)

	June 30, 2017 (Unaudited)	December 31, 2016 (Unaudited)
Assets		
Cash	\$ 80	\$ 84
Interest-earning deposits	103	74
Total cash and cash equivalents	183	158
Investment securities available-for-sale	1,614	1,480
Investment securities held-to-maturity	1,014	1,093
Loans held-for-sale (\$4,473 and \$3,145 measured at fair value, respectively)	4,506	3,177
Loans held-for-investment (\$13 and \$72 measured at fair value, respectively)	6,776	6,065
Loans with government guarantees	278	365
Less: allowance for loan losses	(140)	(142)
Total loans held-for-investment and loans with government guarantees, net	6,914	6,288
Mortgage servicing rights	184	335
Net deferred tax asset	266	286
Federal Home Loan Bank stock	260	180
Premises and equipment, net	299	275
Other assets	725	781
Total assets	\$ 15,965	\$ 14,053
Liabilities and Stockholders' Equity		
Noninterest bearing deposits	\$ 2,012	\$ 2,077
Interest bearing deposits	6,683	6,723
Total deposits	8,695	8,800
Short-term Federal Home Loan Bank advances	3,670	1,780
Long-term Federal Home Loan Bank advances	1,200	1,200
Other long-term debt	493	493
Representation and warranty reserve	20	27
Other liabilities (\$60 and \$60 measured at fair value, respectively)	479	417
Total liabilities	14,557	12,717
Stockholders' Equity		
Common stock \$0.01 par value, 80,000,000 and 70,000,000 shares authorized; 57,161,431 and 56,824,802 shares issued and outstanding, respectively	1	1
Additional paid in capital	1,509	1,503
Accumulated other comprehensive loss	(9)	(7)
Accumulated deficit	(93)	(161)
Total stockholders' equity	1,408	1,336
Total liabilities and stockholders' equity	\$ 15,965	\$ 14,053

The accompanying notes are an integral part of these Consolidated Financial Statements.

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

	Three Months Ended June 30, 2017 2016 (Unaudited)		Six Months Ended June 30, 2017 2016		
Interest Income					
Loans	\$108	\$ 82	\$199	\$ 166	
Investment securities	20	17	39	34	
Interest-earning deposits and other	1	—	1	—	
Total interest income	129	99	239	200	
Interest Expense					
Deposits	12	11	24	22	
Short-term Federal Home Loan Bank advances and other	9	1	12	3	
Long-term Federal Home Loan Bank advances	5	8	11	15	
Other long-term debt	6	2	12	4	
Total interest expense	32	22	59	44	
Net interest income	97	77	180	156	
Provision (benefit) for loan losses	(1) (3) 2	(16)
Net interest income after provision (benefit) for loan losses	98	80	178	172	
Noninterest Income					
Net gain on loan sales	66	90	114	165	
Loan fees and charges	20	19	35	34	
Deposit fees and charges	5	6	9	12	
Loan administration income	6	4	11	10	
Net return (loss) on mortgage servicing rights	6	(4) 20	(10)
Representation and warranty benefit	3	4	7	6	
Other noninterest income	10	9	20	16	
Total noninterest income	116	128	216	233	
Noninterest Expense					
Compensation and benefits	71	66	143	134	
Commissions	16	14	26	24	
Occupancy and equipment	25	21	47	43	
Loan processing expense	14	15	26	27	
Legal and professional expense	8	6	15	15	
Other noninterest expense	20	17	37	33	
Total noninterest expense	154	139	294	276	
Income before income taxes	60	69	100	129	
Provision for income taxes	19	22	32	43	
Net income	\$41	\$ 47	\$68	\$ 86	
Net income per share					
Basic	\$0.72	\$ 0.67	\$1.18	\$ 1.23	
Diluted	\$0.71	\$ 0.66	\$1.16	\$ 1.21	
Weighted average shares outstanding					
Basic	57,101,516	57,796,208	57,012,308	57,442,256	
Diluted	58,138,938	57,751,230	58,106,377	57,623,081	

The accompanying notes are an integral part of these Consolidated Financial Statements.

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Flagstar Bancorp, Inc.
 Consolidated Statements of Comprehensive Income
 (In millions)

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	(Unaudited)			
Net income	\$41	\$47	\$68	\$86
Other comprehensive income (loss), net of tax				
Investment securities	2	1	2	16
Derivatives and hedging activities	(5)	(9)	(4)	(37)
Other comprehensive loss, net of tax	(3)	(8)	(2)	(21)
Comprehensive income	\$38	\$39	\$66	\$65

The accompanying notes are an integral part of these Consolidated Financial Statements.

Flagstar Bancorp, Inc.
 Consolidated Statements of Stockholders' Equity
 (In millions, except share data)

	Preferred Stock		Common Stock			Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Accumulated Deficit)	Total Stockholders' Equity
	Number of Shares Outstand- ing	Amount of Preferred Stock	Number of Shares Outstand- ing	Amount of Common Stock	Additional Paid in Capital			
Balance at December 31, 2015 (Unaudited)	266,657	\$ 267	56,483,258	\$ 1	\$ 1,486	\$ 2	\$ (227)	\$ 1,529
Net income	—	—	—	—	—	—	86	86
Total other comprehensive income (loss)	—	—	—	—	—	(21)	—	(21)
Stock-based compensation	—	—	92,521	—	5	—	—	5
Balance at June 30, 2016	266,657	\$ 267	56,575,779	\$ 1	\$ 1,491	\$ (19)	\$ (141)	\$ 1,599
Balance at December 31, 2016 (Unaudited)	—	\$ —	56,824,802	\$ 1	\$ 1,503	\$ (7)	\$ (161)	\$ 1,336
Net income	—	—	—	—	—	—	68	68
Total other comprehensive income (loss)	—	—	—	—	—	(2)	—	(2)
Warrant exercise	—	—	154,313	—	4	—	—	4
Stock-based compensation	—	—	182,316	—	2	—	—	2
Balance at June 30, 2017	—	\$ —	57,161,431	\$ 1	\$ 1,509	\$ (9)	\$ (93)	\$ 1,408

The accompanying notes are an integral part of these Consolidated Financial Statements.

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Flagstar Bancorp, Inc.

Condensed Consolidated Statements of Cash Flows

(In millions)

	Six Months Ended June 30,	
	2017	2016
	(Unaudited)	
Operating Activities		
Net cash used in operating activities	\$(11,958)	\$(5,153)
Investing Activities		
Proceeds from sale of AFS securities including loans that have been securitized	\$10,853	\$5,943
Collection of principal on investment securities AFS	106	68
Purchase of investment securities AFS and other	(300)	(68)
Collection of principal on investment securities HTM	79	72
Purchase of investment securities HTM and other	—	(15)
Proceeds received from the sale of LHFI	78	228
Net Origination, purchase, and principal repayments of LHFI	(800)	(812)
Purchase of bank owned life insurance	(50)	(85)
Net purchase of FHLB stock	(80)	(2)
Acquisition of premises and equipment, net of proceeds	(48)	(25)
Proceeds from the sale of MSRs	217	21
Other, net	1	9
Net cash provided by investing activities	\$10,056	\$5,334
Financing Activities		
Net change in deposit accounts	\$(105)	\$636
Net change in short term FHLB borrowings and other short term debt	1,890	(1,047)
Proceeds from long term FHLB advances	—	150
Net receipt of payments of loans serviced for others	128	52
Net receipt (disbursement) of escrow payments	14	4
Net cash provided (used) by financing activities	\$1,927	\$(205)
Net increase in cash and cash equivalents	25	(24)
Beginning cash and cash equivalents	158	208
Ending cash and cash equivalents	\$183	\$184
Supplemental disclosure of cash flow information		
Non-cash reclassification of loans originated LHFI to LHFS	\$106	\$1,331
Non-cash reclassification of LHFS to AFS securities	\$10,789	\$5,768
MSRs resulting from sale or securitization of loans	\$103	\$122
Operating section supplemental disclosures		
Cash proceeds from sales of LHFS	\$3,174	\$9,761
Origination, premium paid and purchase of LHFS, net of principal repayments	\$(14,974)	\$(14,639)

The accompanying notes are an integral part of these Consolidated Financial Statements.

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Flagstar Bancorp, Inc.

Notes to the Consolidated Financial Statements (Unaudited)

Note 1 - Basis of Presentation

The accompanying financial statements of Flagstar Bancorp, Inc. ("Flagstar," or the "Company"), including its wholly owned principal subsidiary, Flagstar Bank, FSB (the "Bank"), have been prepared using U.S. GAAP for interim financial statements. Where we say "we," "us," "our," the "Company," "Bancorp" or "Flagstar," we usually mean Flagstar Bancorp, Inc. However, in some cases, a reference to "we," "us," "our," the "Company" or "Flagstar" will include our wholly-owned subsidiary Flagstar Bank, FSB (the "Bank").

These consolidated financial statements do not include all of the information and footnotes required by GAAP for a full year presentation and certain disclosures have been condensed or omitted in accordance with rules and regulations of the SEC. These interim financial statements are unaudited and include, in our opinion, all adjustments necessary for a fair statement of the results for the periods indicated, which are not necessarily indicative of results which may be expected for the full year. These consolidated financial statements and notes should be read in conjunction with the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2016, which is available on our website, at flagstar.com, and on the SEC website, at sec.gov. Certain prior period amounts have been reclassified to conform to the current period presentation.

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Note 2 - Investment Securities

As of June 30, 2017 and December 31, 2016, investment securities were comprised of the following:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(Dollars in millions)				
June 30, 2017				
Available-for-sale securities				
Agency - Commercial	\$522	\$ 1	\$ (5)	\$518
Agency - Residential	1,039	2	(12)	1,029
Municipal obligations	37	—	—	37
Corporate debt obligations	30	—	—	30
Total available-for-sale securities (1)	\$1,628	\$ 3	\$ (17)	\$1,614
Held-to-maturity securities				
Agency - Commercial	\$559	\$ 1	\$ (5)	\$555
Agency - Residential	455	1	(3)	453
Total held-to-maturity securities (1)	\$1,014	\$ 2	\$ (8)	\$1,008
December 31, 2016				
Available-for-sale securities				
Agency - Commercial	\$551	\$ 2	\$ (5)	\$548
Agency - Residential	913	1	(16)	898
Municipal obligations	34	—	—	34
Total available-for-sale securities (1)	\$1,498	\$ 3	\$ (21)	\$1,480
Held-to-maturity securities				
Agency - Commercial	\$595	\$ —	\$ (6)	\$589
Agency - Residential	498	1	(4)	495
Total held-to-maturity securities (1)	\$1,093	\$ 1	\$ (10)	\$1,084

(1) There were no securities of a single issuer, which are not governmental or government-sponsored, that exceeded 10 percent of stockholders' equity at June 30, 2017 or December 31, 2016.

We evaluate AFS and HTM investment securities for other than temporary impairment on a quarterly basis. An OTTI is considered to have occurred when the fair value of a debt security is below its amortized costs and we (1) have the intent to sell the security, (2) will more likely than not be required to sell the security before recovery of its amortized cost, or (3) do not expect to recover the entire amortized cost basis of the security. Investments that have an OTTI are written down through a charge to earnings for the amount representing the credit loss on the security. Gains and losses related to all other factors are recognized in other comprehensive income (loss). During the three and six months ended June 30, 2017 and June 30, 2016, we had no OTTI losses.

Available-for-sale securities

Securities available-for-sale are carried at fair value, with unrealized gains and losses, to the extent they are temporary in nature, reported as a component of other comprehensive income.

We purchased \$77 million and \$300 million of AFS securities, which included U.S. government sponsored agency MBS, corporate debt obligations, and municipal obligations during the three and six months ended June 30, 2017, respectively. We purchased \$40 million and \$68 million of AFS securities, which included U.S. government sponsored agencies comprised of MBS and municipal obligations during the three and six months ended June 30, 2016, respectively.

Gains (losses) on sales of AFS securities are reported in other noninterest income in the Consolidated Statements of Operations. We sold \$62 million of AFS securities during the three and six months ended June 30, 2017, which did not include those related to mortgage loans that had been securitized for sale in the normal course of business. These sales resulted in a realized gain of \$1 million during both the three and six months ended June 30, 2017. During both the three and six months ended June 30, 2016, there were \$175 million in sales of AFS securities, which did not include those related to mortgage loans

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that had been securitized for sale in the normal course of business. These sales resulted in a realized gain of \$1 million during both the three and six months ended June 30, 2016.

Held-to-maturity securities

Investment securities HTM are carried at amortized cost and adjusted for amortization of premiums and accretion of discounts using the interest method. Unrealized losses are not recorded to the extent they are temporary in nature.

Transfers of investment securities into the HTM category from the AFS category are accounted for at fair value on the date of transfer. There were no such transfers during both the three and six months ended June 30, 2017 and June 30, 2016.

There were no purchases of HTM securities during the three and six months ended June 30, 2017. During the three and six months ended June 30, 2016, we purchased zero and \$15 million of HTM securities, respectively. There were no sales of HTM securities during both the three and six months ended June 30, 2017 and June 30, 2016.

The following table summarizes, by duration, the unrealized loss positions on investment securities:

	Unrealized Loss Position with Duration 12 Months and Over		Unrealized Loss Position with Duration Under 12 Months	
	Fair Value	Number of Securities	Fair Value	Number of Securities
	Unrealized Loss		Unrealized Loss	
	(Dollars in millions)			
June 30, 2017				
Available-for-sale securities				
Agency - Commercial	\$5 1	\$	—\$367 30	\$ (5)
Agency - Residential	— —	—	611 49	(12)
Municipal obligations	— —	—	20 7	—
Corporate debt obligations	— —	—	3 1	—
Held-to-maturity securities				
Agency - Commercial	\$4 1	\$	—\$429 27	\$ (5)
Agency - Residential	— —	—	356 44	(3)
December 31, 2016				
Available-for-sale securities				
Agency - Commercial	\$6 1	\$	—\$345 29	\$ (5)
Agency - Residential	— —	—	748 55	(16)
Municipal obligations	— —	—	17 8	—
Held-to-maturity securities				
Agency - Commercial	\$—	\$	—\$528 34	\$ (6)
Agency - Residential	— —	—	385 43	(4)

The amortized cost and estimated fair value of securities are presented below by contractual maturity:

Investment Securities Available-for-Sale			Investment Securities Held-to-maturity		
Amortized Cost	Fair Value	Weighted Average Yield	Amortized Cost	Fair Value	Weighted Average Yield
(Dollars in millions)					

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June 30, 2017

Due after one year through five years	\$16	\$16	3.39	%	\$—	\$—	—	%
Due after five years through 10 years	35	35	5.18	%	61	61	2.50	%
Due after 10 years	1,577	1,563	2.30	%	953	947	2.45	%
Total	\$1,628	\$1,614			\$1,014	\$1,008		

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We pledge investment securities, primarily agency collateralized and municipal taxable mortgage obligations, to collateralize lines of credit and/or borrowings. At June 30, 2017, we had pledged investment securities of \$1.4 billion compared to \$879 million at December 31, 2016.

Note 3 - Loans Held-for-Sale

The majority of our mortgage loans originated as LHFS are sold into the secondary market by securitizing the loans into agency mortgage backed securities or on a whole loan basis. At June 30, 2017 and December 31, 2016, LHFS totaled \$4.5 billion and \$3.2 billion, respectively. For the three and six months ended June 30, 2017, we had net gains on loan sales associated with LHFS of \$66 million and \$114 million, respectively, as compared to \$85 million and \$151 million during the three and six months ended June 30, 2016, respectively.

At June 30, 2017 and December 31, 2016, \$33 million and \$32 million, respectively, of LHFS were recorded at lower of cost or fair value. The remainder of the loans in the portfolio are recorded at fair value as we have elected the fair value option for such loans.

Note 4 - Loans Held-for-Investment

Loans held-for-investment are summarized as follows:

	June 30, 2017	December 31, 2016
	(Dollars in millions)	
Consumer loans		
Residential first mortgage	\$2,538	\$ 2,327
Home equity	459	443
Other	27	28
Total consumer loans	3,024	2,798
Commercial loans		
Commercial real estate (1)	1,557	1,261
Commercial and industrial	1,040	769
Warehouse lending	1,155	1,237
Total commercial loans	3,752	3,267
Total loans held-for-investment	\$6,776	\$ 6,065

(1) Includes \$253 million and \$245 million of owner occupied commercial real estate loans at June 30, 2017 and December 31, 2016, respectively.

During the six months ended June 30, 2017, we sold performing and nonperforming loans with UPB of \$103 million, of which \$25 million were nonperforming. Upon a change in our intent, the loans were transferred to LHFS and subsequently sold resulting in a gain of \$1 million during the six months ended June 30, 2017, which is recorded in net gain on loan sales on the Consolidated Statements of Operations.

During the six months ended June 30, 2016, we sold performing and nonperforming loans with UPB totaling \$1.3 billion, of which \$110 million were nonperforming. Upon a change in our intent, the loans were transferred to LHFS and subsequently sold resulting in a net gain on sale of \$12 million, during the six months ended June 30, 2016, which is recorded in net gain on loan sales on the Consolidated Statements of Operations.

During the six months ended June 30, 2017, we purchased HELOC loans with an UPB of \$75 million. During the six months ended June 30, 2016, we purchased jumbo residential first mortgage loans with an UPB of \$150 million, with a premium of \$1 million.

We have pledged certain LHFI, LHFS, and loans with government guarantees to collateralize lines of credit and/or borrowings with the FHLB of Indianapolis and the FRB of Chicago. At June 30, 2017 and December 31, 2016, we had pledged loans of \$6.8 billion and \$5.3 billion, respectively.

Allowance for Loan Losses

We determine the estimate of the ALLL on at least a quarterly basis. Refer to Note 1 - Description of Business, Basis of Presentation, and Summary of Significant Accounting Policies to the consolidated financial statements in the Annual Report on

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Form 10-K for the year ended December 31, 2016, for a description of the methodology. The ALLL, other than for loans that have been identified for individual evaluation for impairment, is determined on a loan pool basis by grouping loan types with common risk characteristics to determine our best estimate of incurred losses.

The changes in ALLL, by class of loan, are summarized in the following table:

	Residential First Mortgage (1)	Home Equity	Other Consumer	Commercial Real Estate	Commercial and Industrial	Warehouse Lending	Total
(Dollars in millions)							
Three Months Ended June 30, 2017							
Beginning balance ALLL	\$61	\$ 21	\$ 1	\$ 32	\$ 20	\$ 6	\$141
Charge-offs (2)	(1)	(1)	—	—	—	—	(2)
Recoveries	1	1	—	—	—	—	2
Provision (benefit)	(5)	(2)	—	5	1	—	(1)
Ending balance ALLL	\$56	\$ 19	\$ 1	\$ 37	\$ 21	\$ 6	\$140
Three Months Ended June 30, 2016							
Beginning balance ALLL	\$95	\$ 30	\$ 2	\$ 19	\$ 10	\$ 6	\$162
Charge-offs (2)	(8)	(1)	(1)	—	—	—	(10)
Recoveries	1	—	—	—	—	—	1
Provision (benefit)	(7)	1	—	—	1	2	(3)
Ending balance ALLL	\$81	\$ 30	\$ 1	\$ 19	\$ 11	\$ 8	\$150
Six Months Ended June 30, 2017							
Beginning balance ALLL	\$65	\$ 24	\$ 1	\$ 28	\$ 17	\$ 7	\$142
Charge-offs (2)	(5)	(1)	(1)	—	—	—	(7)
Recoveries	1	1	1	—	—	—	3
Provision (benefit)	(5)	(5)	—	9	4	(1)	2
Ending balance ALLL	\$56	\$ 19	\$ 1	\$ 37	\$ 21	\$ 6	\$140
Six Months Ended June 30, 2016							
Beginning balance ALLL	\$116	\$ 32	\$ 2	\$ 18	\$ 13	\$ 6	\$187
Charge-offs (2)	(19)	(3)	(2)	—	—	—	(24)
Recoveries	1	1	1	—	—	—	3
Provision (benefit)	(17)	—	—	1	(2)	2	(16)
Ending balance ALLL	\$81	\$ 30	\$ 1	\$ 19	\$ 11	\$ 8	\$150

(1) Includes allowance and charge-offs related to loans with government guarantees.

Includes charge-offs of zero and \$2 million related to the transfer and subsequent sale of loans during the three months ended June 30, 2017 and June 30, 2016, respectively, and \$1 million and \$8 million during the six months ended June 30, 2017 and June 30, 2016, respectively. Also includes charge-offs related to loans with government guarantees of zero and \$4 million during the three months ended June 30, 2017 and June 30, 2016, respectively, and \$2 million and \$7 million during the six months ended June 30, 2017 and June 30, 2016, respectively.

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The method of evaluation, by class of loan, is summarized in the following table:

	Residential First Mortgage (1)	Home Equity	Other Consumer	Commercial Real Estate	Commercial and Industrial	Warehouse Lending	Total
(Dollars in millions)							
June 30, 2017							
Loans held-for-investment (2)							
Individually evaluated	\$35	\$ 28	\$ —	\$ —	\$ —	\$ —	\$63
Collectively evaluated	2,495	426	27	1,557	1,040	1,155	6,700
Total loans	\$2,530	\$ 454	\$ 27	\$ 1,557	\$ 1,040	\$ 1,155	\$6,763
Allowance for loan losses (2)							
Individually evaluated	\$5	\$ 8	\$ —	\$ —	\$ —	\$ —	\$13
Collectively evaluated	51	11	1	37	21	6	127
Total allowance for loan losses	\$56	\$ 19	\$ 1	\$ 37	\$ 21	\$ 6	\$140
December 31, 2016							
Loans held-for-investment (2)							
Individually evaluated	\$46	\$ 29	\$ —	\$ —	\$ —	\$ —	\$75
Collectively evaluated	2,274	349	28	1,261	769	1,237	5,918
Total loans	\$2,320	\$ 378	\$ 28	\$ 1,261	\$ 769	\$ 1,237	\$5,993
Allowance for loan losses (2)							
Individually evaluated	\$5	\$ 8	\$ —	\$ —	\$ —	\$ —	\$13
Collectively evaluated	60	16	1	28	17	7	129
Total allowance for loan losses	\$65	\$ 24	\$ 1	\$ 28	\$ 17	\$ 7	\$142

(1) Includes allowance related to loans with government guarantees.

(2) Excludes loans carried under the fair value option.

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The following table sets forth the LHFH aging analysis of past due and current loans:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due (1)	Total Past Due	Current	Total LHFH
(Dollars in millions)						
June 30, 2017						
Consumer loans						
Residential first mortgage	\$ 1	\$ 3	\$ 25	\$ 29	\$ 2,509	\$ 2,538
Home equity	1	—	5	6	453	459
Other	—	—	—	—	27	27
Total consumer loans	2	3	30	35	2,989	3,024
Commercial loans						
Commercial real estate	1	—	—	1	1,556	1,557
Commercial and industrial	—	—	—	—	1,040	1,040
Warehouse lending	—	—	—	—	1,155	1,155
Total commercial loans	1	—	—	1	3,751	3,752
Total loans (2)	\$ 3	\$ 3	\$ 30	\$ 36	\$ 6,740	\$ 6,776
December 31, 2016						
Consumer loans						
Residential first mortgage	\$ 6	\$ —	\$ 29	\$ 35	\$ 2,292	\$ 2,327
Home equity	1	2	11	14	429	443
Other	1	—	—	1	27	28
Total consumer loans	8	2	40	50	2,748	2,798
Commercial loans						
Commercial real estate	—	—	—	—	1,261	1,261
Commercial and industrial	—	—	—	—	769	769
Warehouse lending	—	—	—	—	1,237	1,237
Total commercial loans	—	—	—	—	3,267	3,267
Total loans (2)	\$ 8	\$ 2	\$ 40	\$ 50	\$ 6,015	\$ 6,065

(1) Includes loans 90 days or greater past due and performing nonaccrual loans that are less than 90 days past due.

(2) Includes \$4 million and \$13 million of loans 90 days or greater past due, accounted for under the fair value option at June 30, 2017 and December 31, 2016, respectively.

Loans are considered to be past due when any payment of principal or interest is 30 days past the scheduled payment date. While it is the goal of management to collect on loans, we attempt to work out a satisfactory repayment schedule or modification with past due borrowers and will undertake foreclosure proceedings if the delinquency is not satisfactorily resolved. Our practices regarding past due loans are designed to both assist borrowers in meeting their contractual obligations and minimize losses incurred by the Bank.

We cease the accrual of interest on all classes of consumer and commercial loans upon the earlier of, becoming 90 days past due, or when doubt exists as to the ultimate collection of principal or interest (classified as nonaccrual or nonperforming loans). When a loan is placed on nonaccrual status, the accrued interest income is reversed and may only return to accrual status when principal and interest become current and are anticipated to be fully collectible.

Interest income is recognized on nonaccrual loans using a cash basis method. Interest that would have been accrued on impaired loans totaled less than \$1 million and \$1 million during the three and six months ended June 30, 2017, respectively, and less than \$1 million and \$1 million during the three and six months ended June 30, 2016, respectively. At June 30, 2017 and December 31, 2016, we had no loans 90 days past due and still accruing interest.

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Troubled Debt Restructurings

We may modify certain loans in both our consumer and commercial loan portfolios to retain customers or to maximize collection of the outstanding loan balance. We have programs designed to assist borrowers by extending payment dates or reducing the borrower's contractual payments. All loan modifications are made on a case-by-case basis. Our standards relating to loan modifications consider, among other factors, minimum verified income requirements, cash flow analysis, and collateral valuations. TDRs result in those instances in which a borrower demonstrates financial difficulty and for which a concession has been granted, which includes reductions of interest rate, extensions of amortization period, principal and/or interest forgiveness and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of collateral. These loans are classified as nonperforming TDRs if the loan was nonperforming prior to the restructuring, or based upon the results of a contemporaneous credit evaluation. Such loans will continue on nonaccrual status until the borrower has established a willingness and ability to make the restructured payments for at least six months, after which they will be classified as performing TDRs and begin to accrue interest. Performing and nonperforming TDRs remain impaired as interest and principal will not be received in accordance with the original contractual terms of the loan agreement.

Some loan modifications classified as TDRs may not ultimately result in the full collection of principal and interest, as modified, but may give rise to potential incremental losses. We measure impairments using a discounted cash flow method for performing TDRs and measure impairment based on collateral values for nonperforming TDRs.

The following table provides a summary of TDRs by type and performing status:

	TDRs		
	Performing	Nonperforming	Total
	(Dollars in millions)		
June 30, 2017			
Consumer loans (1)			
Residential first mortgage	\$19	\$ 10	\$ 29
Home equity	27	2	29
Total TDRs (2)	\$46	\$ 12	\$ 58
December 31, 2016			
Consumer loans (1)			
Residential first mortgage	\$22	\$ 11	\$ 33
Home equity	45	7	52
Total TDRs (2)	\$67	\$ 18	\$ 85

(1) The ALLL on consumer TDR loans totaled \$11 million and \$9 million at June 30, 2017 and December 31, 2016, respectively.

(2) Includes \$3 million and \$25 million of TDR loans accounted for under the fair value option at June 30, 2017 and December 31, 2016, respectively.

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The following table provides a summary of newly modified TDRs:

	New TDRs		Increase in Allowance at Modification
	Number of Accounts	Pre-Modification Unpaid Principal Balance (1)	
(Dollars in millions)			
Three Months Ended June 30, 2017			
Residential first mortgages	6	\$ 1	\$ 1
Home equity (2)	21	1	1
Other consumer	1	—	—
Total TDR loans	28	\$ 2	\$ 2
Three Months Ended June 30, 2016			
Residential first mortgages	3	\$ 1	\$ 1
Home equity (2)(3)	25	2	2
Total TDR loans	28	\$ 3	\$ 3
Six Months Ended June 30, 2017			
Residential first mortgages	8	\$ 1	\$ 1
Home equity (2)	34	2	2
Other consumer	1	—	—
Total TDR loans	43	\$ 3	\$ 3
Six Months Ended June 30, 2016			
Residential first mortgages	16	\$ 3	\$ 4
Home equity (2)(3)	111	7	6
Commercial and industrial	1	2	1
Total TDR loans	128	\$ 12	\$ 11

(1) Post-modification balances include past due amounts that are capitalized at modification date.

(2) Home equity post-modification unpaid principal balance reflects write downs.

(3) Includes loans carried at the fair value option.

There was one residential first mortgage loan with a UPB of less than \$1 million that was modified in the previous 12 months, which has subsequently defaulted during the three and six months ended June 30, 2017 as compared to one residential first mortgage loan and four home equity loans with a UPB of less than \$1 million for each class which subsequently defaulted during the three and six months ended June 30, 2016. All TDR classes within the consumer and commercial portfolios are considered subsequently defaulted when greater than 90 days past due. There was no increase or decrease in the allowance associated with these TDRs at subsequent default. Subsequent default is defined as a payment re-defaulted within 12 months of the restructuring date.

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Impaired Loans

The following table presents individually evaluated impaired loans and the associated allowance:

	June 30, 2017			December 31, 2016		
	Recorded Investment Balance	Unpaid Principal Balance	Related Allowance	Recorded Investment Balance	Unpaid Principal Balance	Related Allowance
(Dollars in millions)						
With no related allowance recorded						
Consumer loans						
Residential first mortgage	\$ 15	\$ 16	\$ —	\$ 6	\$ 6	\$ —
Total consumer loans with no related allowance recorded	\$ 15	\$ 16	\$ —	\$ 6	\$ 6	\$ —
With an allowance recorded						
Consumer loans						
Residential first mortgage	\$ 20	\$ 19	\$ 5	\$ 40	\$ 40	\$ 5
Home equity	28	28	8	29	29	8
Total consumer loans with an allowance recorded	\$ 48	\$ 47	\$ 13	\$ 69	\$ 69	\$ 13
Total Impaired Consumer loans						
Residential first mortgage	\$ 35	\$ 35	\$ 5	\$ 46	\$ 46	\$ 5
Home equity	28	28	8	29	29	8
Total impaired loans	\$ 63	\$ 63	\$ 13	\$ 75	\$ 75	\$ 13

The following table presents average impaired loans and the interest income recognized:

	Three Months Ended June 30, 2017		2016		Six Months Ended June 30, 2017		2016	
	Average Recorded Investment Balance	Average Interest Income Recognized	Average Recorded Investment Balance	Average Interest Income Recognized	Average Recorded Investment Balance	Average Interest Income Recognized	Average Recorded Investment Balance	Average Interest Income Recognized
(Dollars in millions)								
Consumer loans								
Residential first mortgage	\$ 36	\$ —	\$ 47	\$ —	\$ 39	\$ —	\$ 60	\$ 1
Home equity	27	—	32	1	27	1	32	1
Commercial loans								
Commercial and industrial	—	—	1	—	—	—	3	—
Total impaired loans	\$ 63	\$ —	\$ 80	\$ 1	\$ 66	\$ 1	\$ 95	\$ 2

Credit Quality

We utilize an internal risk rating system which is applied to all consumer and commercial loans. Descriptions of our internal risk ratings as they relate to credit quality follow the ratings used by the U.S. bank regulatory agencies as listed below.

Pass. Pass assets are not impaired nor do they have any known deficiencies that could impact the quality of the asset.

Watch. Watch assets are defined as pass rated assets that exhibit elevated risk characteristics or other factors that deserve management's close attention and increased monitoring. However, the asset does not exhibit a potential or well-defined weakness that would warrant a downgrade to criticized or adverse classification.

Special mention. Assets identified as special mention possess credit deficiencies or potential weaknesses deserving management's close attention. Special mention assets have a potential weakness or pose an unwarranted financial risk that, if not corrected, could weaken the assets and increase risk in the future. Special mention assets are criticized, but do not expose an institution to sufficient risk to warrant adverse classification.

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Substandard. Assets identified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the full collection or liquidation of the debt. They are characterized by the distinct possibility that we will sustain some loss if the deficiencies are not corrected. For home equity loans and other consumer loans, we evaluate credit quality based on the aging and status of payment activity and any other known credit characteristics that call into question full repayment of the asset. Nonperforming loans are classified as either substandard, doubtful or loss.

Doubtful. An asset classified as doubtful has all the weaknesses inherent in one classified substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. A doubtful asset has a high probability of total or substantial loss, but because of specific pending events that may strengthen the asset, its classification as loss is deferred. Doubtful borrowers are usually in default, lack adequate liquidity or capital, and lack the resources necessary to remain an operating entity. Pending events can include mergers, acquisitions, liquidations, capital injections, the perfection of liens on additional collateral, the valuation of collateral, and refinancing. Generally, pending events should be resolved within a relatively short period and the ratings will be adjusted based on the new information. Because of high probability of loss, non-accrual accounting treatment is required for doubtful assets.

Loss. An asset classified as loss is considered uncollectible and of such little value that the continuance as a bankable asset is not warranted. This classification does not mean that an asset has absolutely no recovery or salvage value, but, rather that it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be affected in the future.

Commercial Loans

Management conducts periodic examinations which serve as an independent verification of the accuracy of the ratings assigned. Loan grades are based on different factors within the borrowing relationship: entity sales, debt service coverage, debt/total net worth, liquidity, balance sheet and income statement trends, management experience, business stability, financing structure, and financial reporting requirements. The underlying collateral is also rated based on the specific type of collateral and corresponding LTV. The combination of the borrower and collateral risk ratings results in the final rating for the borrowing relationship.

Consumer Loans

The same rating principles are used for consumer and commercial loans, but the principles are applied differently for consumer loans. Consumer loans consist of open and closed end loans extended to individuals for household, family, and other personal expenditures, and includes consumer loans, and loans to individuals secured by their personal residence, including first mortgage, home equity, and home improvement loans. Because consumer loans are usually relatively small-balance, homogeneous exposures, consumer loans are rated primarily on payment performance. Payment performance is a proxy for the strength of repayment capacity and loans are generally classified based on their payment status rather than by an individual review of each loan.

In accordance with regulatory guidance, we assign risk ratings to consumer loans in the following manner:

- Consumer loans are classified as Watch once the loan becomes 60 days past due.
- Open and closed-end consumer loans 90 days or more past due are classified Substandard.

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	June 30, 2017				
	Pass	Watch	Special Mention	Substandard	Total Loans
	(Dollars in millions)				
Consumer Loans					
Residential First Mortgage	\$2,486	\$ 26	\$ —	—\$ 26	\$2,538
Home equity	428	26	—	5	459
Other Consumer	27	—	—	—	27
Total Consumer Loans	\$2,941	\$ 52	\$ —	—\$ 31	\$3,024
Commercial Loans					
Commercial Real Estate	\$1,525	\$ 24	\$ —	—\$ 8	\$1,557
Commercial and Industrial	967	61	—	12	1,040
Warehouse	1,115	40	—	—	1,155
Total Commercial Loans	\$3,607	\$ 125	\$ —	—\$ 20	\$3,752
	December 31, 2016				
	Pass	Watch	Special Mention	Substandard	Total Loans
	(Dollars in millions)				
Consumer Loans					
Residential First Mortgage	\$2,273	\$ 23	\$ —	\$ 31	\$2,327
Home equity	386	46	—	11	443
Other Consumer	28	—	—	—	28
Total Consumer Loans	\$2,687	\$ 69	\$ —	\$ 42	\$2,798
Commercial Loans					
Commercial Real Estate	\$1,225	\$ 27	\$ 3	\$ 6	\$1,261
Commercial and Industrial	678	59	21	11	769
Warehouse	1,168	16	53	—	1,237
Total Commercial Loans	\$3,071	\$ 102	\$ 77	\$ 17	\$3,267

Note 5 - Loans with Government Guarantees

Substantially all loans with government guarantees are insured or guaranteed by the FHA or the U.S. Department of Veterans Affairs. FHA loans earn interest at a rate based upon the 10-year U.S. Treasury note rate at the time the underlying loan becomes delinquent, which is not paid by the FHA until claimed. Certain loans within our portfolio may be subject to indemnifications and insurance limits which exposes us to limited credit risk. We have reserved for these risks within other assets and as a component of our ALLL on residential first mortgages.

At June 30, 2017 and December 31, 2016, respectively, loans with government guarantees totaled \$278 million and \$365 million.

At June 30, 2017 and December 31, 2016, respectively, repossessed assets and the associated claims recorded in other assets totaled \$99 million and \$135 million.

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Note 6 - Variable Interest Entities

We have no consolidated VIEs as of June 30, 2017 and December 31, 2016.

We have a continuing involvement, but are not the primary beneficiary for one unconsolidated VIE related to the FSTAR 2007-1 mortgage securitization trust. In accordance with the settlement agreement with MBIA, there is no further recourse to us related to FSTAR 2007-1, unless MBIA fails to meet their obligations. At June 30, 2017 and December 31, 2016, the FSTAR 2007-1 mortgage securitization trust included 2,170 loans and 2,453 loans, respectively, with an aggregate principal balance of \$76 million and \$89 million, respectively.

Note 7 - Mortgage Servicing Rights

We have investments in MSR that result from the sale of loans to the secondary market for which we retain the servicing. The primary risk associated with MSRs is the potential reduction in fair value as a result of higher than anticipated prepayments due to loan refinancing prompted, in part, by declining interest rates or government intervention. Conversely, these assets generally increase in value in a rising interest rate environment to the extent that prepayments are slower than previously anticipated. We utilize derivatives as economic hedges to offset changes in the fair value of the MSRs resulting from the actual or anticipated changes in prepayments stemming from changing interest rate environments. There is also a risk of valuation decline due to higher than expected increases in default rates, which we do not believe can be effectively managed using derivatives. For further information, See Note 8 - Derivative Financial Instruments, regarding the derivative instruments utilized to manage our MSR risks.

Changes in the carrying value of residential first mortgage MSRs, accounted for at fair value, were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(Dollars in millions)			
Balance at beginning of period	\$295	\$281	\$335	\$296
Additions from loans sold with servicing retained	82	65	103	122
Reductions from sales	(191)	—	(256)	(24)
Changes in fair value due to (1)				
Decrease in MSR due to payoffs, pay-downs and run-off	(4)	(15)	(10)	(26)
Changes in estimates of fair value (2)	2	(30)	12	(67)
Balance at end of period	\$184	\$301	\$184	\$301

(1) Changes in fair value are included within net return (loss) on MSRs on the Consolidated Statements of Operations.

(2) Represents estimated MSR value change resulting primarily from market-driven changes.

The following table summarizes the hypothetical effect on the fair value of servicing rights using adverse changes of 10 percent and 20 percent to the weighted average of certain significant assumptions used in valuing these assets. The significant assumptions used in the fair value measurement of the MSRs are option adjusted spread and prepayment rate. Significant increases (decreases) in both of these assumptions in isolation would result in a significantly lower (higher) fair value measurement.

	June 30, 2017		December 31, 2016	
	Fair value after		Fair value after	
Actual	10% adverse	20% adverse	Actual	10% adverse

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	change		change	
	(Dollars in millions)			
Option adjusted spread	6.41	% \$176 \$ 172	7.78	% \$326 \$ 318
Constant prepayment rate	9.41	% 173 166	16.68	% 322 311
Weighted average annual cost to service per loan	\$70.49	178 176	\$68.18	330 326

The sensitivity calculations above are hypothetical and should not be considered to be predictive of future performance. Changes in fair value based on adverse changes in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. To isolate the effect of the specified change, the fair value shock analysis is consistent with the identified adverse change, while holding all other assumptions

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constant. In practice, a change in one assumption generally impacts other assumptions, which may either magnify or counteract the effect of the change. For further fair value disclosures relating to MSR's, see Note 17 - Fair Value Measurements.

Contractual servicing and subservicing fees. Contractual servicing and subservicing fees, including late fees and other ancillary income are presented below. Contractual servicing fees are included within net (loss) return on MSR's on the Consolidated Statements of Operations. Contractual subservicing fees including late fees and other ancillary income are included within loan administration income on the Consolidated Statements of Operations. Subservicing fee income is recorded for fees earned, net of third party subservicing costs, for loans subserviced.

The following table summarizes income and fees associated with contractual servicing rights:

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	2017	2016	2017	2016
	(Dollars in millions)			
Net return (loss) on mortgage servicing rights				
Servicing fees, ancillary income and late fees (1)	\$9	\$21	\$29	\$38
Changes in fair value	(2)	(45)	2	(93)
Net return (loss) on MSR derivatives (2)	5	19	(3)	45
Net transaction costs	(6)	1	(8)	—
Total net return (loss) on mortgage servicing rights	\$6	\$(4)	\$20	\$(10)

(1) Servicing fees are recorded on the accrual basis. Ancillary income and late fees are recorded on a cash basis.

(2) Changes in the derivatives utilized as economic hedges to offset changes in fair value of the MSR's.

The following table summarizes income and fees associated with our mortgage loans subserviced:

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	2017	2016	2017	2016
	(Dollars in millions)			
Loan administration income on mortgage loans subserviced				
Servicing fees, ancillary income and late fees (1)	\$9	\$7	\$17	\$14
Other servicing charges	(3)	(3)	(6)	(4)
Total income on mortgage loans subserviced, included in loan administration	\$6	\$4	\$11	\$10

(1) Servicing fees are recorded on the accrual basis. Ancillary income and late fees are recorded on cash basis.

Note 8 - Derivative Financial Instruments

Derivative financial instruments are recorded at fair value in other assets and other liabilities on the Consolidated Statements of Financial Condition. The Company's policy is to present its derivative assets and derivative liabilities on the Consolidated Statement of Financial Condition on a gross basis, even when provisions allowing for setoff are in place. However, for derivative contracts cleared through certain central clearing parties, variation margin payments are recognized as settlements. We are exposed to non-performance risk by the counterparties to our various derivative financial instruments. A majority of our derivatives are centrally cleared through a Central Counterparty Clearing House or consist of residential mortgage interest rate lock commitments further limiting our exposure to non-performance risk. We believe that the non-performance risk inherent in our remaining derivative contracts is

minimal based on credit standards and the collateral provisions of the derivative agreements.

Derivatives not designated as hedging instruments: We maintain a derivative portfolio of interest rate swaps, futures and forward commitments used to manage exposure to changes in interest rates, MSR asset values and to meet the needs of customers. We also enter into interest rate lock commitments, which are commitments to originate mortgage loans whereby the interest rate on the loan is determined prior to funding and the customers have locked into that interest rate. Market risk on interest rate lock commitments and mortgage LHFS is managed using corresponding forward sale commitments.

Derivatives designated as hedging instruments: We have designated certain interest rate swaps as cash flow hedges of certain interest rate payments of our variable-rate FHLB advances.

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Changes in the fair value of derivatives designated as cash flow hedges are recorded in other comprehensive income (loss) on the Consolidated Statement of Financial Condition and reclassified into interest expense in the same period in which the hedge transaction is recognized in earnings. At June 30, 2017, we had \$3 million (net-of-tax) of unrealized losses on derivatives designated as cash flow hedges recorded in accumulated other comprehensive income (loss), compared to \$1 million of unrealized gains at December 31, 2016. The estimated amount to be reclassified from other comprehensive income into earnings during the next 12 months represents \$4 million of losses (net-of-tax).

Derivatives that are designated in hedging relationships are assessed for effectiveness using regression analysis at inception and throughout the hedge period. All hedge relationships were and are expected to be highly effective as of June 30, 2017. Cash flows and the profit impact associated with designated hedges are reported in the same line item as the underlying hedged item.

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The notional amount, estimated fair value and maturity of our derivative financial instruments were as follows:

	June 30, 2017 (1)		
	Notional Amount	Fair Value	Expiration Dates
	(2)	(2)	
	(Dollars in millions)		
Derivatives designated as hedging instruments:			
Assets			
Interest rate swaps on FHLB advances	\$830	\$ 2	2023-2026
Derivatives not designated as hedging instruments:			
Assets			
Futures	\$ 138	\$ —	2018-2022
Mortgage backed securities forwards	5,844	24	2017
Rate lock commitments	4,677	27	2017
Interest rate swaps and swaptions	1,340	15	2017-2027
Total derivative assets	\$11,999	\$ 66	
Liabilities			
Futures	\$2,266	\$ 1	2017-2022
Mortgage backed securities forwards	1,090	4	2017
Rate lock commitments	531	1	2017
Interest rate swaps	779	2	2017-2047
Total derivative liabilities	\$4,666	\$ 8	
December 31, 2016			
	Notional Amount	Fair Value	Expiration Dates
	(2)	(2)	
	(Dollars in millions)		
Derivatives designated as hedging instruments:			
Assets			
Interest rate swaps on FHLB advances	\$600	\$ 20	2023-2026
Liabilities			
Interest rate swaps on FHLB advances	\$230	\$ 1	2025-2026
Derivatives not designated as hedging instruments:			
Assets			
Futures	\$4,621	\$ 2	2017-2020
Mortgage backed securities forwards	3,776	43	2017
Rate lock commitments	3,517	24	2017
Interest rate swaps and swaptions	2,231	35	2017-2033
Total derivative assets	\$14,145	\$ 104	
Liabilities			
Futures	\$134	\$ —	2017
Mortgage backed securities forwards	1,893	11	2017
Rate lock commitments	598	6	2017
Interest rate swaps	1,129	37	2017-2047
Total derivative liabilities	\$3,754	\$ 54	

At June 30, 2017, variation margin pledged to or received from a Central Counterparty Clearing House to cover the prior day's fair value of open positions is considered settlement of the derivative position for accounting purposes. At December 31, 2016, variation margin was not recognized as settlement.

- (1) Derivative assets and liabilities are included in other assets and other liabilities on the Consolidated Statements of Financial Condition, respectively.

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The following tables present the derivatives subject to a master netting arrangement, including the cash pledged as collateral:

	Gross Amounts Netted in the Statement of Gross Financial Amounts Position (Dollars in millions)	Net Amount Presented in the Statement of Financial Position	Gross Amounts Not Offset in the Statement of Financial Position Cash Collateral
June 30, 2017			
Derivatives designated as hedging instruments:			
Assets			
Interest rate swaps on FHLB advances (1)	\$2	\$ —	\$ 2
	\$ —	\$ 2	\$ —
	\$ 2	\$ —	\$ 27
Derivatives not designated as hedging instruments:			
Assets			
Mortgage backed securities forwards	\$24	\$ —	\$ 24
Interest rate swaps and swaptions (1)	15	—	15
	\$ —	\$ 15	\$ —
Total derivative assets	\$39	\$ —	\$ 39
	\$ —	\$ 39	\$ —
	\$ 39	\$ —	\$ 13
Liabilities			
Futures	\$1	\$ —	\$ 1
Mortgage backed securities forwards	4	—	4
Interest rate swaps and swaptions (1)	2	—	2
	\$ —	\$ 2	\$ —
Total derivative liabilities	\$7	\$ —	\$ 7
	\$ —	\$ 7	\$ —
	\$ 7	\$ —	\$ 18
December 31, 2016			
Derivatives designated as hedging instruments:			
Assets			
Interest rate swaps on FHLB advances (1)	\$20	\$ 1	\$ 19
	\$ —	\$ 1	\$ —
	\$ 19	\$ —	\$ —
Liabilities			
Interest rate swaps on FHLB advances (1)	\$1	\$ 1	\$ —
	\$ —	\$ 1	\$ —
	\$ 1	\$ —	\$ 33
Derivatives not designated as hedging instruments:			
Assets			
Futures	\$2	\$ —	\$ 2
Mortgage-backed securities forwards	43	\$ —	43
Interest rate swaps and swaptions (1)	35	—	35
	\$ —	\$ 35	\$ —
Total derivative assets	\$80	\$ —	\$ 80
	\$ —	\$ 80	\$ —
	\$ 80	\$ —	\$ 74
Liabilities			
Futures	\$—	\$ —	\$ —
Mortgage-backed securities forwards	11	—	11
Interest rate swaps and swaptions (1)	37	—	37
	\$ —	\$ 37	\$ —
Total derivative liabilities	\$48	\$ —	\$ 48
	\$ —	\$ 48	\$ —
	\$ 48	\$ —	\$ 21

(1) At June 30, 2017, variation margin pledged to or received from a Central Counterparty Clearing House to cover the prior day's fair value of open positions is considered settlement of the derivative position for accounting purposes.

At December 31, 2016, variation margin was not recognized as settlement and we had an additional \$15 million in variation margin in excess of the amounts disclosed above.

We pledged a total of \$18 million of cash collateral on derivative liabilities and \$27 million of maintenance margin on derivative assets to counterparties and had an obligation to return cash of \$13 million on derivative assets at June 30, 2017. We pledged a total of \$54 million of cash collateral to counterparties and had an obligation to return cash of \$74 million at December 31, 2016 for derivative activities. The net cash pledged is included in other assets on the Consolidated Statements of Financial Condition.

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Changes in fair value of derivatives not designated as hedging instruments are recognized in the Consolidated Statements of Income.

The net gain (loss) recognized in income on derivative instruments, net of the impact of offsetting positions, were as follows:

		Three Months Ended June 30, 2017	Six Months Ended June 30, 2016	2017	2016
		(Dollars in millions)			
Derivatives not designated as hedging instruments:	Location of Gain/(Loss)				
Futures	Net return (loss) on mortgage servicing rights	\$—	\$1	\$—	\$4
Interest rate swaps and swaptions	Net return (loss) on mortgage servicing rights	3	13	(5)	28
Mortgage-backed securities forwards	Net return (loss) on mortgage servicing rights	3	5	3	13
Rate lock commitments and forward agency and loan sales	Net gain (loss) on loan sales	41	(6)	(8)	(1)
Rate lock commitments	Other noninterest income	—	—	—	1
Interest rate swaps (1)	Other noninterest income	1	(1)	1	1
Total derivative gain (loss)		\$48	\$12	\$(9)	\$46

(1) Includes customer-initiated commercial interest rate swaps.

Note 9 - Borrowings

Federal Home Loan Bank Advances

The following is a breakdown of our FHLB advances outstanding:

	June 30, 2017		December 31, 2016	
	Amount	Rate	Amount	Rate
	(Dollars in millions)			
Short-term fixed rate term advances	\$3,670	1.14%	\$1,780	0.62%
Total Short-term Federal Home Loan Bank advances	3,670		1,780	
Long-term LIBOR adjustable advances	1,025	1.41%	1,025	1.12%
Long-term fixed rate advances (1)	175	1.12%	175	1.12%
Total Long-term Federal Home Loan Bank advances	1,200		1,200	
Total Federal Home Loan Bank advances	\$4,870		\$2,980	

(1) Includes the current portion of fixed rate advances of \$175 million and \$50 million at June 30, 2017 and December 31, 2016, respectively.

We are required to maintain a minimum amount of qualifying collateral. In the event of default, the FHLB advance is similar to a secured borrowing, whereby the FHLB has the right to sell the pledged collateral to settle the fair value of the outstanding advances.

At June 30, 2017, we had the authority and approval from the FHLB to utilize a line of credit of up to \$7.0 billion and we may access that line to the extent that collateral is provided. At June 30, 2017, we had \$4.9 billion of advances outstanding and an additional \$798 million of collateralized borrowing capacity available at the FHLB. The advances can be collateralized by non-delinquent single-family residential first mortgage loans, loans with government guarantees, certain other loans and investment securities.

At June 30, 2017, \$1.0 billion of the outstanding advances were long-term adjustable rate, with interest rates that reset every three months and are based on the three-month LIBOR index. The advances may be prepaid without penalty, with notification at scheduled three month intervals after an initial 12 month lockout period which is based on the settlement date of each advance. The outstanding advances included \$830 million in a cash flow hedge relationship as discussed in Note 8 - Derivative Financial Instruments.

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The following table contains detailed information on our FHLB advances and other borrowings:

	Three Months		Six Months Ended	
	Ended June 30,		June 30,	
	2017	2016	2017	2016
	(Dollars in millions)			
Maximum outstanding at any month end	\$4,870	\$2,646	\$4,870	\$3,557
Average outstanding balance	4,629	2,460	3,830	2,841
Average remaining borrowing capacity	1,042	983	1,356	843
Weighted average interest rate	1.22 %	1.42 %	1.20 %	1.25 %

The following table outlines the maturity dates of our FHLB advances and other borrowings:

	June 30, 2017
	(Dollars in millions)
2017	\$ 3,720
2018	125
2019	—
2020	—
Thereafter	1,025
Total	\$ 4,870

Parent Company Senior Notes and Trust Preferred Securities

The following table presents long-term debt, net of debt issuance costs:

	June 30, 2017		December 31, 2016	
	Amount	Interest Rate	Amount	Interest Rate
	(Dollars in millions)			
Senior Notes				
Senior notes, matures 2021	\$246	6.125 %	\$246	6.125 %
Trust Preferred Securities				
Floating Three Month LIBOR				
Plus 3.25%, matures 2032	\$26	4.55 %	\$26	4.25 %
Plus 3.25%, matures 2033	26	4.41 %	26	4.13 %
Plus 3.25%, matures 2033	26	4.40 %	26	4.25 %
Plus 2.00%, matures 2035	26	3.16 %	26	2.88 %
Plus 2.00%, matures 2035	26	3.16 %	26	2.88 %
Plus 1.75%, matures 2035	51	3.00 %	51	2.71 %
Plus 1.50%, matures 2035	25	2.66 %	25	2.38 %
Plus 1.45%, matures 2037	25	2.70 %	25	2.41 %
Plus 2.50%, matures 2037	16	3.75 %	16	3.46 %
Total Trust Preferred Securities	247		247	
Total other long-term debt	\$493		\$493	

Senior Notes

On July 11, 2016, we issued \$250 million of senior notes (“2021 Senior Notes”) which mature on July 15, 2021. The proceeds from these notes were used to bring dividends current and redeem our outstanding Series C Preferred Stock. The notes are unsecured and rank equally and ratably with the unsecured senior indebtedness of Flagstar Bancorp, Inc.

Prior to June 15, 2021, we may redeem some or all of the 2021 Senior Notes at a redemption price equal to the greater of 100 percent of the aggregate principal amount of the notes to be redeemed or the sum of the present values of the remaining

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scheduled payments discounted to the redemption date on a semi-annual basis using a discount rate equal to the Treasury Rate plus 0.50 percent, plus, in each case accrued and unpaid interest.

Trust Preferred Securities

We sponsor nine trust subsidiaries, which issued preferred stock to third party investors. We issued trust preferred securities to those trusts, which we have included in long-term debt. The trust preferred securities are the sole assets of those trusts.

The trust preferred securities are callable by us at any time. Interest is payable quarterly; however, we may defer interest payments for up to 20 quarters without default or penalty. As of June 30, 2017, we had no deferred interest.

Note 10 - Representation and Warranty Reserve

At the time a loan is sold, an estimate of the fair value of the guarantee associated with the mortgage loans is recorded in the representation and warranty reserve in the Consolidated Statements of Financial Condition which reduces the net gain on loan sales in the Consolidated Statements of Operations.

The following table shows the activity impacting the representation and warranty reserve:

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	2017	2016	2017	2016
	(Dollars in millions)			
Balance at beginning of period	\$23	\$40	\$27	\$40
Provision (benefit)				
Gain on sale reduction for representation and warranty liability	1	1	2	3
Representation and warranty provision (benefit)	(3)	(4)	(7)	(6)
Total	(2)	(3)	(5)	(3)
(Charge-offs) recoveries, net	(1)	(1)	(2)	(1)
Balance at end of period	\$20	\$36	\$20	\$36

Note 11 - Warrants and Restricted Stock Units

May Investor Warrant

We granted warrants (the "May Investor Warrants") on January 30, 2009 under anti-dilution provisions applicable to certain investors (the "May Investors") in our May 2008 private placement capital raise.

During the six months ended June 30, 2017, a total of 237,627 May Investor Warrants were exercised, resulting in the net issuance of 154,313 shares of Common Stock and the liability amounted to zero. There are no remaining May Investor Warrants outstanding as of June 30, 2017.

At December 31, 2016, the liability was \$4 million. For further information, see Note 17 - Fair Value Measurements.

TARP Warrant

On January 30, 2009, in conjunction with the sale of 266,657 shares of Series C fixed rate cumulative non-convertible perpetual preferred stock ("Series C Preferred Stock") for \$267 million, we issued a warrant to purchase up to approximately 645,138 shares of Common Stock at an exercise price of \$62.00 per share (the "Warrant").

The Warrant is exercisable through January 30, 2019 and remains outstanding.

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Restricted Stock and Restricted Stock Units

We had stock-based compensation expense of \$2 million and \$6 million for the three and six months ended June 30, 2017.

The following table summarizes restricted stock and restricted stock units activity:

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2017	
	Shares	Weighted — Average Grant-Date Fair Value per Share	Shares	Weighted — Average Grant-Date Fair Value per Share
Restricted Stock				
Non-vested balance at beginning of period	1,465,893	\$ 18.00	1,461,910	\$ 17.68
Granted	240,446	29.06	326,338	28.41
Vested	(134,229)	17.54	(213,941)	18.96
Canceled and forfeited	(116,783)	17.85	(118,980)	17.93
Non-vested balance at end of period	1,455,327	\$ 19.88	1,455,327	\$ 19.88

Note 12 - Accumulated Other Comprehensive Income (Loss)

The following table sets forth the components in accumulated other comprehensive income (loss):

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2016	
	2017	2016	2017	2016
(Dollars in millions)				
Investment securities				
Beginning balance	\$(8)	\$20	\$(8)	\$5
Unrealized gain (loss)	2	2	2	26
Less: Tax (benefit) provision	1	1	1	10
Net unrealized gain (loss)	1	1	1	16
Reclassifications out of AOCI (1)	2	—	2	—
Less: Tax (benefit) provision	1	—	1	—
Net unrealized gain (loss) reclassified out of AOCI	1	—	1	—
Other comprehensive income/(loss), net of tax	2	1	2	16
Ending balance	\$(6)	\$21	\$(6)	\$21
Cash Flow Hedges				
Beginning balance	\$2	\$(31)	\$1	\$(3)
Unrealized gain (loss)	(4)	(15)	(2)	(63)
Less: Tax (benefit) provision	(2)	(3)	(1)	(19)
Net unrealized gain (loss)	(2)	(12)	(1)	(44)
Reclassifications out of AOCI (1)	(5)	3	(5)	7
Less: Tax (benefit) provision	(2)	—	(2)	—
Net unrealized gain (loss) reclassified out of AOCI	(3)	3	(3)	7
Other comprehensive income/(loss), net of tax	(5)	(9)	(4)	(37)
Ending balance	\$(3)	\$(40)	\$(3)	\$(40)

(1) Reclassifications are reported in other noninterest income on the Consolidated Statement of Operations.

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Note 13 - Earnings Per Share

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

The following table sets forth the computation of basic and diluted earnings per share of common stock:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(Dollars in millions, except share data)			
Net income	\$41	\$ 47	\$68	\$ 86
Deferred cumulative preferred stock dividends	—	(8)	—	(16)
Net income applicable to common stockholders	\$41	\$ 39	\$68	\$ 70
Weighted average shares				
Weighted average common shares outstanding	57,101,816	57,796,208	57,012,208	54,256,208
Effect of dilutive securities				
May Investor Warrants	—	349,539	24,575	327,307
Stock-based awards	1,037,132	2,895,518	1,069,287	1,518,518
Weighted average diluted common shares	58,138,948	57,512,300	58,106,670	56,230,811
Earnings per common share				
Basic earnings per common share	\$0.72	\$ 0.67	\$ 1.18	\$ 1.23
Effect of dilutive securities				
May Investor Warrants	—	—	—	—
Stock-based awards	(0.01)	(0.01)	(0.02)	(0.02)
Diluted earnings per common share	\$0.71	\$ 0.66	\$ 1.16	\$ 1.21

Under the terms of the Series C Preferred Stock the Company elected to defer payments of preferred stock dividends beginning with the February 2012 dividend. Although, while being deferred, the impact was not included in quarterly net income from continuing operations, the deferral did impact net income applicable to common stock for the purpose of calculating earnings per share, as shown above. On July 29, 2016, we completed the \$267 million redemption of our Series C Preferred Stock.

Note 14 - Income Taxes

The provision for income taxes in interim periods requires us to make a best estimate of the effective tax rate expected to be applicable for the full year, adjusted for any discreet items for the applicable period. This estimated effective tax rate is then applied to interim consolidated pre-tax operating income to determine the interim provision for income taxes.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(Dollars in millions)			
Provision for income taxes	\$19	\$22	\$32	\$43
Effective tax provision rate	31.8%	32.7%	32.3%	33.4%

We believe that it is unlikely that our unrecognized tax benefits will change by a material amount during the next 12 months. We recognize interest and penalties related to unrecognized tax benefits in provision for income taxes.

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Note 15 - Regulatory Matters

Regulatory Capital

We, along with the Bank, must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary actions by regulators that could have a material effect on the Consolidated Financial Statements. On January 1, 2015, the Basel III rules became effective and include transition provisions through 2018.

To be categorized as "well-capitalized," the Company and the Bank must maintain minimum tangible capital, Tier 1 capital, common equity Tier 1, and total capital ratios as set forth in the table below. We, along with the Bank, are considered "well-capitalized" at both June 30, 2017 and December 31, 2016.

The following tables present the regulatory capital ratios as of the dates indicated:

Bancorp	Actual		For Capital Adequacy Purposes			Well Capitalized Under Prompt Corrective Action Provisions		
	Amount	Ratio	Amount	Ratio		Amount	Ratio	
(Dollars in millions)								
June 30, 2017								
Tangible capital (to adjusted avg. total assets)	\$1,408	9.10 %	N/A	N/A		N/A	N/A	
Tier 1 leverage (to adjusted avg. total assets)	1,408	9.10 %	\$ 619	4.00 %	%	\$ 773	5.00 %	%
Common equity Tier 1 capital (to RWA)	1,196	12.45 %	432	4.50 %	%	625	6.50 %	%
Tier 1 capital (to RWA)	1,408	14.65 %	577	6.00 %	%	769	8.00 %	%
Total capital (to RWA)	1,530	15.92 %	769	8.00 %	%	961	10.00 %	%
December 31, 2016								
Tangible capital (to adjusted avg. total assets)	\$1,256	8.88 %	N/A	N/A		N/A	N/A	
Tier 1 leverage (to adjusted avg. total assets)	1,256	8.88 %	\$ 566	4.0 %	%	\$ 707	5.0 %	%
Common equity Tier 1 capital (to RWA)	1,084	13.06 %	374	4.5 %	%	540	6.5 %	%
Tier 1 capital (to RWA)	1,256	15.12 %	498	6.0 %	%	664	8.0 %	%
Total capital (to RWA)	1,363	16.41 %	664	8.0 %	%	830	10.0 %	%
N/A - Not applicable								
Bank	Actual		For Capital Adequacy Purposes			Well Capitalized Under Prompt Corrective Action Provisions		
	Amount	Ratio	Amount	Ratio		Amount	Ratio	
(Dollars in millions)								
June 30, 2017								
Tangible capital (to adjusted avg. total assets)	\$1,590	10.26 %	N/A	N/A		N/A	N/A	
Tier 1 leverage (to adjusted avg. total assets)	1,590	10.26 %	\$ 620	4.00 %	%	\$ 775	5.00 %	%
Common equity tier 1 capital (to RWA)	1,590	16.49 %	434	4.50 %	%	627	6.50 %	%
Tier 1 capital (to RWA)	1,590	16.49 %	579	6.00 %	%	772	8.00 %	%
Total capital (to RWA)	1,712	17.75 %	772	8.00 %	%	964	10.00 %	%
December 31, 2016								
Tangible capital (to adjusted avg. total assets)	\$1,491	10.52 %	N/A	N/A		N/A	N/A	

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Tier 1 leverage (to adjusted avg. total assets)	1,491	10.52%	\$ 567	4.0	%	\$ 709	5.0	%
Common equity tier 1 capital (to RWA)	1,491	17.90%	375	4.5	%	542	6.5	%
Tier 1 capital (to RWA)	1,491	17.90%	500	6.0	%	667	8.0	%
Total capital (to RWA)	1,598	19.18%	667	8.0	%	833	10.0	%

N/A - Not applicable

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Note 16 - Legal Proceedings, Contingencies and Commitments

Legal Proceedings

We and our subsidiaries are subject to various pending or threatened legal proceedings arising out of the normal course of business operations. In addition, the Bank is routinely named in civil actions throughout the country by borrowers and former borrowers relating to the origination, purchase, sale, and servicing of mortgage loans. From time to time, governmental agencies also conduct investigations or examinations of various practices of the Bank. In the course of such investigations or examinations, the Bank cooperates with such agencies and provides information as requested.

We assess the liabilities and loss contingencies in connection with pending or threatened legal and regulatory proceedings on at least a quarterly basis and establish accruals when we believe it is probable that a loss may be incurred and that the amount of such loss can be reasonably estimated. Once established, litigation accruals are adjusted, as appropriate, in light of additional information.

At June 30, 2017, we do not believe that the amount of any reasonably possible losses in excess of any amounts accrued with respect to ongoing proceedings or any other known claims will be material to our financial statements, or that the ultimate outcome of these actions will have a material adverse effect on our financial condition, results of operations or cash flows.

DOJ litigation settlement

In 2012, the Bank entered into a Settlement Agreement with the DOJ which meets the definition of a financial liability (the "DOJ Liability").

In accordance with the Settlement Agreement, we made an initial payment of \$15 million and agreed to make future annual payments totaling \$118 million in annual increments of up to \$25 million upon meeting all conditions, which are evaluated quarterly and include: (a) the reversal of the DTA valuation allowance, which occurred at the end of 2013; (b) the repayment of the Fixed Rate Cumulative Perpetual Preferred Stock, Series C (the "TARP Preferred"), which occurred in the third quarter of 2016; and (c) the Bank's Tier 1 Leverage Capital Ratio equals 11 percent or greater as filed in the Call Report with the OCC.

No payment would be required until six months after the Bank files its Call Report OCC first reporting that its Tier 1 Leverage Capital Ratio was 11 percent or greater. If all other conditions were then satisfied, an initial annual payment would be due at that time. The next annual payment is only made if such other conditions continue to be satisfied otherwise payments are delayed until all such conditions are met. Further, making such a payment must not violate any material banking regulatory requirement, and the OCC must not object in writing.

Consistent with our business and regulatory requirements, Flagstar shall seek in good faith to fulfill the conditions, and will not undertake any conduct or fail to take any action the purpose of which is to frustrate or delay our ability to fulfill any of the above conditions.

Additionally, if the Bank and Bancorp become party to a business combination in which the Bank or Bancorp represent less than 33.3 percent of the resulting company's assets. Annual payments must commence twelve months after the date of that business combination.

We elected to account for the DOJ Liability under the fair value option. To determine the fair value, we utilize a discounted cash flow model. Key assumptions for the discounted cash flow model include using a discount rate as of

June 30, 2017 of 9.0 percent; probability weightings of multiple cash flow scenarios and possible outcomes which contemplate the above conditions and estimates of forecasted net income, size of the balance sheet, capital levels, dividends and their impact on the timing of cash payments and the assumptions we believe a market participant would make to transfer the liability. The fair value of the DOJ Liability was \$60 million at both June 30, 2017 and December 31, 2016.

Other litigation accruals

At June 30, 2017 and December 31, 2016, excluding the fair value liability relating to the DOJ litigation settlement, our total accrual for contingent liabilities, settled litigation and regulatory matters was \$3 million.

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Commitments

A summary of the contractual amount of significant commitments is as follows:

	June 30, December 31,	
	2017	2016
	(Dollars in millions)	
Commitments to extend credit		
Mortgage loans interest-rate lock commitments	\$5,208	\$ 4,115
Warehouse loan commitments	1,400	1,670
Commercial and industrial commitments	678	424
Other commercial commitments	814	651
HELOC commitments	217	179
Other consumer commitments	46	57
Standby and commercial letters of credit	44	30

Commitments to extend credit are agreements to lend to a customer as long as there is not a violation of any condition established in the contract. Since many of these commitments expire without being drawn upon, the total commitment amounts do not necessarily represent future cash flow requirements. Commitments generally have fixed expiration dates or other termination clauses. We evaluate each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by us, upon extension of credit is based on management's credit evaluation of the counterparties.

These instruments involve, to varying degrees, elements of credit and interest rate risk beyond the amount recognized on the Consolidated Statements of Financial Condition. Our exposure to credit losses in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. We utilize the same credit policies in making commitments and conditional obligations as we do for balance sheet instruments. The types of credit we extend are as follows:

Mortgage loan interest-rate lock commitments. We enter into mortgage interest-rate lock commitments with our customers. These commitments are considered to be derivative instruments and the fair value of these commitments is recorded in the Consolidated Statements of Financial Condition in other assets. For further information, see Note 8 - Derivative Financial Instruments.

Warehouse loan commitments. Lines of credit provided to mortgage originators to fund loans they originate and then sell. The proceeds of the sale of the loans are used to repay the draw on the line used to fund the loans.

Commercial and industrial and other commercial commitments. Conditional commitments issued under various terms to lend funds to business and other entities. These commitments include revolving credit agreements, term loan commitments and short-term borrowing agreements. Many of these loan commitments have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of these commitments are expected to expire without being funded, the total commitment amounts do not necessarily represent future liquidity requirements.

HELOC commitments. Commitments to extend, originate or purchase credit are primarily lines of credit to consumers and have specified rates and maturity dates. Many of these commitments also have adverse change clauses, which allow us to cancel the commitment due to deterioration in the borrowers' creditworthiness or a decline in the collateral value.

Other consumer commitments. Conditional commitments issued to accommodate the financial needs of customers. The commitments are under various terms to lend funds to consumers, which include revolving credit agreements, term loan commitments and short-term borrowing agreements.

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

We maintain a reserve for the estimate of probable credit losses inherent in unfunded commitments to extend credit. Unfunded commitments to extend credit include unfunded loans with available balances, new commitments to lend that are not

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yet funded, and standby and commercial letters of credit. A reserve balance of \$2 million, at June 30, 2017 and \$3 million at December 31, 2016 is reflected in other liabilities on the Consolidated Statements of Financial Condition.

Note 17 - Fair Value Measurements

We utilize fair value measurements to record or disclose the fair value on certain assets and liabilities. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability through an orderly transaction between market participants at the measurement date. The determination of fair values of financial instruments often requires the use of estimates. In cases where quoted market values in an active market are not available, we use present value techniques and other valuation methods to estimate the fair values of our financial instruments. These valuation models rely on market-based parameters when available, such as interest rate yield curves or credit spreads. Unobservable inputs may be based on management's judgment, assumptions and estimates related to credit quality, our future earnings, interest rates and other relevant inputs. These valuation methods require considerable judgment and the resulting estimates of fair value can be significantly affected by the assumptions made and methods used. Refer to Note 22 - Fair Value Measurements to the consolidated financial statements of the Annual Report on Form 10-K for the year ended December 31, 2016, for a description of our valuation methodologies and information about the fair value hierarchy.

Valuation Hierarchy

U.S. GAAP establishes a three-level valuation hierarchy for disclosure of fair value measurements. The hierarchy is based on the transparency of the inputs used in the valuation process with the highest priority given to quoted prices available in active markets and the lowest priority to unobservable inputs where no active market exists, as discussed below.

Level 1 - Quoted prices (unadjusted) for identical assets or liabilities in active markets in which we can participate as of the measurement date;

Level 2 - Quoted prices for similar instruments in active markets, and other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument; and

Level 3 - Unobservable inputs that reflect our own assumptions about the assumptions that market participants would use in pricing an asset or liability.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input within the valuation hierarchy that is significant to the overall fair value measurement. Transfers between levels of the fair value hierarchy are recognized at the end of the reporting period.

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Assets and Liabilities Measured at Fair Value on a Recurring Basis.

The following tables present the financial instruments carried at fair value by caption on the Consolidated Statement of Financial Condition and by level in the valuation hierarchy.

	June 30, 2017			Total Fair Value
	Level 1	Level 2	Level 3	
	(Dollars in millions)			
Investment securities available-for-sale				
Agency - Commercial	\$—	\$518	\$—	\$ 518
Agency - Residential	—	1,029	—	1,029
Municipal obligations	—	37	—	37
Corporate debt obligations	—	30	—	30
Loans held-for-sale				
Residential first mortgage loans	—	4,473	—	4,473
Loans held-for-investment				
Residential first mortgage loans	—	8	—	8
Home equity	—	—	5	5
Mortgage servicing rights	—	—	184	184
Derivative assets				
Rate lock commitments (fallout-adjusted)	—	—	27	27
Mortgage-backed securities forwards	—	24	—	24
Interest rate swaps and swaptions	—	15	—	15
Interest rate swap on FHLB advances (net)	—	2	—	2
Total assets at fair value	\$—	\$6,136	\$216	\$ 6,352
Derivative liabilities				
Rate lock commitments (fallout-adjusted)	\$—	\$—	\$(1)	\$(1)
Futures	(1)	—	—	(1)
Mortgage backed securities forwards	—	(4)	—	(4)
Interest rate swaps	—	(2)	—	(2)
DOJ litigation settlement	—	—	(60)	(60)
Contingent consideration	—	—	(23)	(23)
Total liabilities at fair value	\$(1)	\$(6)	\$(84)	\$(91)

On May 15, 2017, the Company closed on the acquisition of certain assets of Opes Advisors (“Opes”), a California based retail mortgage originator and wealth management service provider. Although the acquired assets of Opes were not significant, the addition of Opes positions us to increase our distributed retail lending channel. Consideration in the acquisition of Opes consisted of upfront cash and contingent cash in the form of an earn-out. The earn-out is based on future target production volumes and profitability of the division which were significant inputs to the preliminary fair value. The acquisition resulted in goodwill of \$16 million net of the deferred tax impact of the contingent consideration. We deem the initial valuation of the assets and liabilities to be provisional and have left the measurement period open. These fair values may be adjusted in a future period, not to exceed one year after the acquisition date, to reflect new facts and circumstances which existed as of the acquisition date.

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	December 31, 2016			Total
	Level 1	Level 2	Level 3	Fair Value
	(Dollars in millions)			
Investment securities available-for-sale				
Agency - Commercial	\$—	\$548	\$—	\$548
Agency - Residential	—	898	—	898
Municipal obligations	—	34	—	34
Loans held-for-sale				
Residential first mortgage loans	—	3,145	—	3,145
Loans held-for-investment				
Residential first mortgage loans	—	7	—	7
Home equity	—	—	65	65
Mortgage servicing rights	—	—	335	335
Derivative assets				
Rate lock commitments (fallout-adjusted)	—	—	24	24
Futures	2	—	—	2
Mortgage backed securities forwards	—	43	—	43
Interest rate swaps and swaptions	—	35	—	35
Interest rate swaps on FHLB advances (net)	—	19	—	19
Total assets at fair value	\$2	\$4,729	\$424	\$5,155
Derivative liabilities				
Rate lock commitments (fallout-adjusted)	\$—	\$—	\$(6)	\$(6)
Mortgage backed securities forwards	—	(11)	—	(11)
Interest rate swaps	—	(37)	—	(37)
Warrant liabilities	—	(4)	—	(4)
DOJ litigation settlement	—	—	(60)	(60)
Total liabilities at fair value	\$—	\$(52)	\$(66)	\$(118)

There were no transfers between Level 1 and Level 2 during the six months ended June 30, 2017.

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Fair Value Measurements Using Significant Unobservable Inputs

The tables below include a roll forward of the Consolidated Statements of Financial Condition amounts (including the change in fair value) for financial instruments classified by us within level 3 of the valuation hierarchy:

	Balance at Beginning of Period	Recorded in Earnings		Recorded in OCI		Purchases / Originations	Sales	Settlements	Transfers In (Out)	Balance at End of Period
		Total Unrealized Gains / (Losses)	Total Realized Gains / (Losses)	Total Unrealized Gains / (Losses)	Total Unrealized Gains / (Losses)					
(Dollars in millions)										
Three Months Ended June 30, 2017										
Assets										
Loans held-for-sale										
Home equity	\$53	\$ —	\$ —	\$ —	\$ —	\$ (52)	\$ (1)	\$ —	\$ —	\$ —
Loans held-for-investment										
Home equity	5	—	—	—	—	—	—	—	—	5
Mortgage servicing rights	295	(2)	—	—	82	(191)	—	—	—	184
Rate lock commitments (net) (1)	41	18	—	—	64	—	—	(97)	—	26
Totals	\$394	\$ 16	\$ —	\$ —	\$ 146	\$ (243)	\$ (1)	\$ (97)	\$ —	\$ 215
Liabilities										
DOJ litigation settlement	\$(60)	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$(60)
Contingent consideration	—	—	—	—	(23)	—	—	—	—	(23)
Totals	\$(60)	\$ —	\$ —	\$ —	\$(23)	\$ —	\$ —	\$ —	\$ —	\$(83)
Three Months Ended June 30, 2016										
Assets										
Loans held-for-investment										
Home equity	\$95	\$ (3)	\$ —	\$ —	\$ —	\$ —	\$ (10)	\$ —	\$ —	\$ 82
Mortgage servicing rights	281	(44)	—	—	64	—	—	—	—	301
Rate lock commitments (net) (1)	61	58	—	—	90	—	—	(126)	—	83
Totals	\$437	\$ 11	\$ —	\$ —	\$ 154	\$ —	\$ (10)	\$ (126)	\$ —	\$ 466
Liabilities										
DOJ litigation settlement	\$(84)	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$(84)

(1) Rate lock commitments are reported on a fallout adjusted basis. Transfers out of Level 3 represent the settlement value of the commitments that are transferred to LHFS, which are classified as Level 2 assets.

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	Recorded in Earnings		Recorded in OCI		Purchases / Originations	Sales	Settlements	Transfers at In (Out)	Balance at End of Period
	Total Unrealized Gains / (Losses)	Total Realized Gains / (Losses)	Total Unrealized Gains / (Losses)	Total					
Six Months Ended June 30, 2017									
Assets									
Loans held-for-sale									
Home equity	\$—	\$ 1	\$ —	—\$	—\$ —	\$(52)	\$(1)	\$ 52	\$—
Loans held-for-investment									
Home equity	65	1	—	—	—	—	(6)	(55)	5
Mortgage servicing rights	335	2	—	—	103	(256)	—	—	184
Rate lock commitments (net) (1)	18	34	—	—	117	—	—	(143)	26
Totals	\$418	\$ 38	\$ —	—\$	—\$ 220	\$(308)	\$(7)	\$(146)	\$ 215
Liabilities									
DOJ litigation settlement	\$(60)	\$ —	\$ —	—\$	—\$ —	\$—	\$ —	\$—	\$(60)
Contingent consideration	—	—	—	—	(23)	—	—	—	(23)
Totals	\$(60)	\$ —	\$ —	—\$	—\$ (23)	\$—	\$ —	\$—	\$(83)
Six Months Ended June 30, 2016									
Assets									
Loans held-for-investment									
Home equity	\$106	\$(2)	\$ —	—\$	—\$ —	\$—	\$(22)	\$—	\$ 82
Mortgage servicing rights	296	(92)	—	—	121	(24)	—	—	301
Rate lock commitments (net) (1)	26	120	—	—	157	—	—	(220)	83
Totals	\$428	\$ 26	\$ —	—\$	—\$ 278	\$(24)	\$(22)	\$(220)	\$ 466
Liabilities									
DOJ litigation settlement	\$(84)	\$ —	\$ —	—\$	—\$ —	\$—	\$ —	\$—	\$(84)

(1) Rate lock commitments are reported on a fallout adjusted basis. Transfers out of Level 3 represent the settlement value of the commitments that are transferred to LHFS, which are classified as Level 2 assets.

We utilized swaptions futures, forward agency and loan sales and interest rate swaps to manage the risk associated with MSR's and rate lock commitments. Gains and losses for individual lines in the tables do not reflect the effect of our risk management activities related to such level 3 instruments.

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The following tables present the quantitative information about recurring level 3 fair value financial instruments and the fair value measurements as of:

	Fair Value	Valuation Technique	Unobservable Input	Range (Weighted Average)
	(Dollars in millions)			
June 30, 2017				
Assets				
Loans held-for-investment				
Home equity	\$5	Discounted cash flows	Discount rate Constant prepayment rate Constant default rate Option adjusted spread	5.8% - 10.8% (9.0%) 5.0% - 7.5% (6.3%) 3.0% - 4.5% (3.4%) 5.2% - 7.7% (6.4%)
Mortgage servicing rights	\$184	Discounted cash flows	Constant prepayment rate Weighted average cost to service per loan	7.6% - 11.2% (9.4%) \$56 - \$82 (\$70)
Rate lock commitments (net)	\$26	Consensus pricing	Origination pull-through rate	66.6% - 100.0% (83.3%)
Liabilities				
DOJ litigation settlement	\$60	Discounted cash flows	Discount rate Asset growth rate	7.2% - 10.8% (9.0%) 1.0% - 18.1% (3.7%)
Contingent consideration	\$23	Discounted cash flows	Beta Equity volatility	0.6 - 1.6 (1.1) 26.6% - 58.9% (40.0%)
		Fair Value Valuation Technique (Dollars in millions)	Unobservable Input	Range (Weighted Average)
December 31, 2016				
Assets				
Loans held-for-investment				
Home equity	\$65	Discounted cash flows	Discount rate Constant prepayment rate Constant default rate Option adjusted spread	6.0% - 12.2% (9.3%) 16.3% - 24.4% (20.3%) 2.7% - 4.1% (3.7%) 6.2% - 9.3% (7.8%)
Mortgage servicing rights	\$335	Discounted cash flows	Constant prepayment rate Weighted average cost to service per loan	13.9% - 19.2% (16.7%) \$55 - \$82 (\$68)
Rate lock commitments (net)	\$18	Consensus pricing	Origination pull-through rate	66.9% - 100.0% (83.6%)
Liabilities				
DOJ litigation settlement	\$60	Discounted cash flows	Discount rate Asset growth rate	6.6% - 9.8% (8.2%) 4.2% - 11.6% (7.9%)

Recurring Significant Unobservable Inputs

The significant unobservable inputs used in the fair value measurement of the home equity loans are discount rates, constant prepayment rates, and default rates. The constant prepayment and default rates are based on a 12 month historical average. Significant increases (decreases) in the discount rate in isolation would result in a significantly lower (higher) fair value measurement. Increases (decreases) in prepay rates in isolation result in a higher (lower) fair value and increases (decreases) in default rates in isolation result in a lower (higher) fair value. HELOC loans formerly included in the FSTAR 2005-1 and FSTAR 2006-1 securitization trusts, also classified as home equity loans,

were valued utilizing a loan-level discounted cash flow model which projects expected cash flows given three potential outcomes: (1) paid-in-full at scheduled maturity, (2) default at scheduled maturity (foreclosure), and (3) modification at scheduled maturity into an amortizing HELOC. Loans are placed into the potential outcome buckets based on their underlying current delinquency, FICO scores and property CLTV all of which are unobservable inputs. These loans were sold in the second quarter of 2017.

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The significant unobservable inputs used in the fair value measurement of the MSR's are option adjusted spreads, prepayment rates, and cost to service. Significant increases (decreases) in all three assumptions in isolation would result in a significantly lower (higher) fair value measurement. Additionally, the key economic assumptions used in determining the changes in fair value of MSR's capitalized were as follows:

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2016	
Weighted average life (in years)	6.1	7.0	6.2	7.0
Weighted average constant prepayment rate	9.8%	13.3%	10.1%	13.5%
Weighted average option adjusted spread	6.0%	8.9%	6.9%	8.2%

The key economic assumptions reflected in the overall fair value of the entire portfolio of MSR's were as follows:

	June 30, 2017		December 31, 2016	
Weighted average life (in years)	6.2		6.6	
Weighted average constant prepayment rate	9.4%		16.7%	
Weighted average option adjusted spread	6.4%		7.8%	

The significant unobservable input used in the fair value measurement of the DOJ litigation settlement is the discount rate and asset growth rate, in addition to those discussed in Note 16 - Legal Proceedings, Contingencies and Commitments. Significant increases (decreases) in the discount rate or asset growth rate in isolation would result in a marginally lower (higher) fair value measurement. For further information on the fair value inputs related to the DOJ litigation, see Note 16 - Legal Proceedings, Contingencies, and Commitments.

The significant unobservable input used in the fair value measurement of the rate lock commitments is the pull through rate. The pull through rate is a statistical analysis of our actual rate lock fallout history to determine the sensitivity of the residential mortgage loan pipeline compared to interest rate changes and other deterministic values. New market prices are applied based on updated loan characteristics and new fallout ratios (i.e., the inverse of the pull through rate) are applied accordingly. Significant increases (decreases) in the pull through rate in isolation would result in a significantly higher (lower) fair value measurement.

The significant unobservable input used in the fair value of the contingent consideration is future forecasted target production volumes and profitability of the division. An increase or decrease to these inputs results in an increase or decrease of the liability. Other unobservable inputs include Beta and volatility which drive the risk adjusted discount rate utilized in a Monte Carlo simulation. An increase or decrease in these inputs results in a decrease or increase to the liability.

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Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

We also have assets that under certain conditions are subject to measurement at fair value on a nonrecurring basis. Assets measured at fair value on a nonrecurring basis were as follows:

	Total	Level	Level	Gains/(Losses)
	(1)	2	3	
	(Dollars in millions)			
June 30, 2017				
Loans held-for-sale (2)	\$9	\$ 9	\$ —	\$ (1)
Impaired loans held-for-investment (2)				
Residential first mortgage loans	21	—	21	(4)
Repossessed assets (3)	9	—	9	—
Totals	\$39	\$ 9	\$ 30	\$ (5)
December 31, 2016				
Loans held-for-sale (2)	\$9	\$ 9	\$ —	\$ (2)
Impaired loans held-for-investment (2)				
Residential first mortgage loans	25	—	25	(28)
Repossessed assets (3)	14	—	14	(2)
Totals	\$48	\$ 9	\$ 39	\$ (32)

(1) The fair values are determined at various dates during the six months ended June 30, 2017 and the year ended December 31, 2016, respectively.

(2) Gains/(losses) reflect fair value adjustments on assets for which we did not elect the fair value option.

(3) Gains/(losses) reflect write downs of repossessed assets based on the estimated fair value of the specific assets.

The following tables present the quantitative information about nonrecurring level 3 fair value financial instruments and the fair value measurements:

	Fair Value	Valuation Technique	Unobservable Input	Range (Weighted Average)
	(Dollars in millions)			
June 30, 2017				
Impaired loans held-for-investment				
Residential first mortgage loans	\$21	Fair value of collateral	Loss severity discount	27% - 29% (28.0%)
Repossessed assets	\$9	Fair value of collateral	Loss severity discount	12% - 100% (73.8%)
December 31, 2016				
Impaired loans held-for-investment				
Residential first mortgage loans	\$25	Fair value of collateral	Loss severity discount	22% - 40% (29.5%)
Repossessed assets	\$14	Fair value of collateral	Loss severity discount	22% - 100% (69.5%)

Nonrecurring Significant Unobservable Inputs

The significant unobservable inputs used in the fair value measurement of the impaired loans and repossessed assets are appraisals or other third-party price evaluations which incorporate measures such as recent sales prices for comparable properties.

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Fair Value of Financial Instruments

The following table presents the carrying amount and estimated fair value of financial instruments that are carried either at fair value, cost, or amortized cost:

	June 30, 2017				
	Carrying Value	Estimated Fair Value			
Total		Level 1	Level 2	Level 3	
(Dollars in millions)					
Assets					
Cash and cash equivalents	\$183	\$183	\$183	\$—	\$ —
Investment securities available-for-sale	1,614	1,614	—	1,614	—
Investment securities held-to-maturity	1,014	1,008	—	1,008	—
Loans held-for-sale	4,506	4,674	—	4,674	—
Loans held-for-investment	6,776	6,867	—	8	6,859
Loans with government guarantees	278	269	—	269	—
Mortgage servicing rights	184	184	—	—	184
Federal Home Loan Bank stock	260	260	—	260	—
Bank owned life insurance	325	325	—	325	—
Repossessed assets	9	9	—	—	9
Other assets, foreclosure claims	99	99	—	99	—
Derivative financial instruments, assets	68	68	—	41	27
Liabilities					
Retail deposits					
Demand deposits and savings accounts	\$(5,394)	\$(4,998)	\$—	\$(4,998)	\$ —
Certificates of deposit	(1,153)	(1,159)	—	(1,159)	—
Government deposits	(851)	(834)	—	(834)	—
Company controlled deposits	(1,297)	(994)	—	(994)	—
Federal Home Loan Bank advances	(4,870)	(4,856)	—	(4,856)	—
Long-term debt	(493)	(382)	—	(382)	—
DOJ litigation settlement	(60)	(60)	—	—	(60)
Contingent consideration	(23)	(23)	—	—	(23)
Derivative financial instruments, liabilities	(8)	(8)	(1)	(6)	(1)

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	December 31, 2016				
	Carrying Value	Estimated Fair Value			
Total		Level 1	Level 2	Level 3	
(Dollars in millions)					
Assets					
Cash and cash equivalents	\$ 158	\$ 158	\$ 158	\$ —	\$ —
Investment securities available-for-sale	1,480	1,480	—	1,480	—
Investment securities held-to-maturity	1,093	1,084	—	1,084	—
Loans held-for-sale	3,177	3,178	—	3,178	—
Loans held-for-investment	6,065	5,998	—	7	5,991
Loans with government guarantees	365	354	—	354	—
Mortgage servicing rights	335	335	—	—	335
Federal Home Loan Bank stock	180	180	—	180	—
Bank owned life insurance	271	271	—	271	—
Repossessed assets	14	14	—	—	14
Other assets, foreclosure claims	135	135	—	135	—
Derivative financial instruments, assets	123	123	45	54	24
Liabilities					
Retail deposits					
Demand deposits and savings accounts	\$(5,268)	\$(4,956)	\$—	\$(4,956)	\$ —
Certificates of deposit	(1,056)	(1,062)	—	(1,062)	—
Government deposits	(1,030)	(1,011)	—	(1,011)	—
Company controlled deposits	(1,446)	(1,371)	—	(1,371)	—
Federal Home Loan Bank advances	(2,980)	(2,964)	—	(2,964)	—
Long-term debt	(493)	(277)	—	(277)	—
Warrant liabilities	(4)	(4)	—	(4)	—
DOJ litigation settlement	(60)	(60)	—	—	(60)
Derivative financial instruments, liabilities	(54)	(54)	(11)	(37)	(6)

The methods and assumptions used by us in estimating fair value of financial instruments which are required for disclosure only, are as follows:

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

Investment securities held-to-maturity. Fair values are generated using market inputs, where possible, including quoted prices (the closing price in an exchange market), bid prices (the price at which a buyer stands ready to purchase), and other market information.

Loans held-for-investment. The fair value is estimated using internally developed discounted cash flow models using market interest rate inputs as well as management's best estimate of spreads for similar collateral.

Loans with government guarantees. The fair value is estimated by using internally developed discounted cash flow models using market interest rate inputs as well as management's best estimate of spreads for similar collateral.

Federal Home Loan Bank stock. No secondary market exists for FHLB stock. The stock is bought and sold at par by the FHLB. Management believes that the recorded value equals the fair value.

Bank owned life insurance. The fair value of bank owned life insurance policies is based on the cash surrender values of the policies as reported by the insurance companies.

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Other assets, foreclosure claims. The fair value of foreclosure claims with government guarantees approximates the carrying amount.

Deposit accounts. The fair value of deposits with no defined maturity is estimated based on a discounted cash flow model that incorporates current market rates for similar products and expected attrition. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for certificates of deposit with similar remaining maturities.

Federal Home Loan Bank advances. Rates currently available for debt with similar terms and remaining maturities are used to estimate the fair value of the existing debt.

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

Fair Value Option

We elected the fair value option for certain items as discussed throughout the Notes to the Consolidated Financial Statements to mitigate a divergence between accounting losses and economic exposure. Interest income on LHFS is accrued on the principal outstanding primarily using the "simple-interest" method.

The following table reflects the change in fair value included in earnings of financial instruments for which the fair value option has been elected:

	Three Months Ended June 30, 2017	2016	Six Months Ended June 30, 2017	2016
	(Dollars in millions)			

Assets

Loans held-for-sale				
Net gain on loan sales	\$115	\$145	\$168	\$289
Loans held-for-investment				
Other non-interest income	\$—	\$2	\$1	\$2

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The following table reflects the difference between the aggregate fair value and aggregate remaining contractual principal balance outstanding for assets and liabilities for which the fair value option has been elected:

	June 30, 2017			December 31, 2016		
	Unpaid Principal Balance	Fair Value	Fair Value Over / (Under) Unpaid Principal Balance	Unpaid Principal Balance	Fair Value	Fair Value Over / (Under) Unpaid Principal Balance
(Dollars in millions)						
Assets						
Nonaccrual loans						
Loans held-for-sale	\$4	\$3	\$ (1)	\$2	\$2	\$ —
Loans held-for-investment	6	4	(2)	19	13	(6)
Total nonaccrual loans	\$10	\$7	\$ (3)	\$21	\$15	\$ (6)
Other performing loans						
Loans held-for-sale	\$4,327	\$4,470	\$ 143	\$3,103	\$3,143	\$ 40
Loans held-for-investment	10	9	(1)	72	59	(13)
Total other performing loans	\$4,337	\$4,479	\$ 142	\$3,175	\$3,202	\$ 27
Total loans						
Loans held-for-sale	\$4,331	\$4,473	\$ 142	\$3,105	\$3,145	\$ 40
Loans held-for-investment	16	13	(3)	91	72	(19)
Total loans	\$4,347	\$4,486	\$ 139	\$3,196	\$3,217	\$ 21
Liabilities						
Litigation settlement (1)	\$(118)	\$(60)	\$ 58	\$(118)	\$(60)	\$ 58

(1) We are obligated to pay \$118 million in installment payments upon meeting certain performance conditions, as described in Note 16 - Legal Proceedings, Contingencies and Commitments.

Note 18 - Segment Information

Our operations are conducted through three operating segments: Community Banking, Mortgage Originations, and Mortgage Servicing. The Other segment includes the remaining reported activities. Operating segments are defined as components of an enterprise that engage in business activity from which revenues are earned and expenses incurred for which discrete financial information is available that is evaluated regularly by executive management in deciding how to allocate resources and in assessing performance. The operating segments have been determined based on the products and services offered and reflect the manner in which financial information is currently evaluated by management. Each segment operates under the same banking charter, but is reported on a segmented basis for this report. Each of the operating segments is complementary to each other and because of the interrelationships of the segments, the information presented is not indicative of how the segments would perform if they operated as independent entities.

Effective January 1, 2017, activity related to Loans with Government Guarantees, was moved from the Mortgage Servicing segment to the Mortgage Originations segment and we began to allocate the tax provision at a segment level. Prior to this change, the tax provision was reflected in the Other segment. The statutory federal tax rate is used for Community Banking, Mortgage Originations, and Mortgage Servicing segments with the difference between the statutory rate and the effective tax rate held in the Other segment. Prior period segment financial information, related to both changes, has been recast to conform to the current presentation.

The Community Banking segment originates loans, provides deposits and fee based services to consumer, business, and mortgage lending customers through its Branch Banking, Business Banking and Commercial Banking, Government Banking, Warehouse Lending and LHFII Portfolio groups. Products offered through these groups include checking accounts, savings accounts, money market accounts, certificates of deposit, consumer loans, commercial loans, commercial real estate loans, equipment finance and leasing, home builder finance loans and warehouse lines of credit. Other financial services available include consumer and corporate card services, customized treasury management solutions, merchant services and capital markets services such as loan syndications.

The Mortgage Originations segment originates, acquires and sells one-to-four family residential mortgage loans. The origination and acquisition of mortgage loans comprises the majority of the lending activity. Mortgage loans are originated

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through home loan centers, national call centers, the Internet and unaffiliated banks and mortgage banking and brokerage companies, where the net interest income and the gains from sales associated with these loans are recognized in the Mortgage Originations segment.

The Mortgage Servicing segment services and subservices mortgage loans, on a fee basis, for others. Also, the Mortgage Servicing segment services, on a fee basis, residential LHFH mortgages held by the Community Banking segment and MSR's held by the Mortgage Originations segment. The Mortgage Servicing segment may also collect ancillary fees, such as late fees, and earns income through the use of noninterest-bearing escrows.

The Other segment includes the treasury functions, funding revenue associated with stockholders' equity, the impact of interest rate risk management, the impact of balance sheet funding activities, and miscellaneous other expenses of a corporate nature. Treasury functions include administering the investment securities portfolios, balance sheet funding, and interest rate risk management. In addition, the Other segment includes revenue and expenses related to treasury and corporate assets and liabilities and equity not directly assigned or allocated to the Mortgage Originations, Mortgage Servicing or Community Banking operating segments.

Revenues are comprised of net interest income (before the provision (benefit) for loan losses) and noninterest income. Noninterest expenses and provision (benefit) for income taxes, are fully allocated to each operating segment. Allocation methodologies may be subject to periodic adjustment as the internal management accounting system is revised and the business or product lines within the segments change.

The following tables present financial information by business segment for the periods indicated:

	Three Months Ended June 30, 2017				
	Community Banking	Mortgage Originations	Mortgage Servicing	Other	Total
	(Dollars in millions)				
Summary of Operations					
Net interest income	\$57	\$ 32	\$ 4	\$ 4	\$97
Net gain (loss) on loan sales	(1)	67	—	—	66
Representation and warranty benefit	—	3	—	—	3
Other noninterest income	6	21	15	5	47
Total net interest income and noninterest income	62	123	19	9	213
(Provision) benefit for loan losses	—	—	—	1	1
Depreciation and amortization expense	(2)	(1)	(1)	(5)	(9)
Other noninterest expense	(45)	(75)	(24)	(1)	(145)
Total noninterest expense	(47)	(76)	(25)	(6)	(154)
Income (loss) before income taxes	15	47	(6)	4	60
Provision (benefit) for income taxes	5	17	(3)	—	19
Net income (loss)	\$10	\$ 30	\$ (3)	\$ 4	\$41
Intersegment revenue	\$—	\$ 1	\$ 3	\$(4)	\$—
Average balances					
Loans held-for-sale	\$15	\$ 4,254	\$ —	\$ —	\$4,269
Loans with government guarantees	—	295	—	—	295
Loans held-for-investment	6,188	7	—	29	6,224
Total assets	6,255	5,562	39	3,854	15,710
Deposits	7,362	—	1,377	—	8,739

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	Three Months Ended June 30, 2016				
	Commercial Banking	Mortgage Originations	Mortgage Servicing	Other	Total
	(Dollars in millions)				
Summary of Operations					
Net interest income	\$49	\$ 21	\$ 6	\$ 1	\$77
Net gain (loss) on loan sales	3	87	—	—	90
Representation and warranty benefit	—	4	—	—	4
Other noninterest income	6	9	13	6	34
Total net interest income and noninterest income	58	121	19	7	205
(Provision) benefit for loan losses	3	—	—	—	3
Depreciation and amortization expense	(2)	(1)	(1)	(4)	(8)
Other noninterest expense	(45)	(62)	(21)	(3)	(131)
Total noninterest expense	(47)	(63)	(22)	(7)	(139)
Income (loss) before income taxes	14	58	(3)	—	69
Provision (benefit) for income taxes	5	20	(1)	(2)	22
Net income (loss)	\$9	\$ 38	\$ (2)	\$ 2	\$47
Intersegment revenue	\$—	\$ —	\$ 6	\$ (6)	\$—
Average balances					
Loans held-for-sale	\$56	\$ 2,828	\$ —	\$ —	\$2,884
Loans with government guarantees	—	444	—	—	444
Loans held-for-investment	5,566	3	—	—	5,569
Total assets	5,653	4,109	40	3,636	13,438
Deposits	7,073	—	1,558	—	8,631

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	Six Months Ended June 30, 2017				Total
	Community Banking	Mortgage Originations	Mortgage Servicing	Other	
(Dollars in millions)					
Summary of Operations					
Net interest income	\$108	\$ 62	\$ 9	\$1	\$180
Net gain (loss) on loan sales	(3)	117	—	—	114
Representation and warranty benefit	—	7	—	—	7
Other noninterest income	14	43	29	9	95
Total net interest income and noninterest income	119	229	38	10	396
(Provision) benefit for loan losses	(2)	(2)	—	2	(2)
Depreciation and amortization expense	(4)	(3)	(2)	(9)	(18)
Other noninterest expense	(89)	(137)	(49)	(1)	(276)
Total noninterest expense	(93)	(140)	(51)	(10)	(294)
Income (loss) before income taxes	24	87	(13)	2	100
Provision (benefit) for income taxes	8	31	(5)	(2)	32
Net income (loss)	\$16	\$ 56	\$ (8)	\$4	\$68
Intersegment revenue	\$(1)	\$ 1	\$ 9	\$(9)	\$—
Average balances					
Loans held-for-sale	\$18	\$ 3,762	\$ —	\$—	\$3,780
Loans with government guarantees	—	318	—	—	318
Loans held-for-investment	5,898	6	—	29	5,933
Total assets	5,966	5,085	40	3,790	14,881
Deposits	7,408	—	1,359	—	8,767
Six Months Ended June 30, 2016					
	Community Banking	Mortgage Originations	Mortgage Servicing	Other	Total
(Dollars in millions)					
Summary of Operations					
Net interest income	\$96	\$ 43	\$ 10	\$7	\$156
Net gain (loss) on loan sales	9	156	—	—	165
Representation and warranty benefit	—	6	—	—	6
Other noninterest income	13	11	28	10	62
Total net interest income and noninterest income	118	216	38	17	389
(Provision) benefit for loan losses	16	—	—	—	16
Depreciation and amortization expense	(4)	(2)	(2)	(7)	(15)
Other noninterest expense	(88)	(122)	(45)	(6)	(261)
Total noninterest expense	(92)	(124)	(47)	(13)	(276)
Income (loss) before income taxes	42	92	(9)	4	129
Provision (benefit) for income taxes	15	32	(3)	(1)	43
Net income (loss)	\$27	\$ 60	\$ (6)	\$5	\$86
Intersegment revenue	\$(1)	\$ —	\$ 12	\$(11)	\$—
Average balances					
Loans held-for-sale	\$117	\$ 2,780	\$ —	\$—	\$2,897
Loans with government guarantees	—	460	—	—	460
Loans held-for-investment	5,611	7	—	—	5,618

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Total assets	5,745	4,071	41	3,634	13,491
Deposits	6,984	—	1,357	—	8,341

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Note 19 - Recently Issued Accounting Pronouncements

Adoption of New Accounting Standards

We adopted the following accounting standard updates (ASU) during 2017, none of which had a material impact to our financial statements:

Standard	Description	Effective Date
ASU 2016-17	Consolidation (Topic 810): Interests Held Through Related Parties That are Under Common Control	January 1, 2017
ASU 2016-09	Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting	January 1, 2017
ASU 2016-07	Investments - Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting	January 1, 2017
ASU 2016-06	Derivatives and Hedging (Topic 815): Contingent Put and Call Options in Debt Instruments	January 1, 2017
ASU 2016-05	Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Relationships	January 1, 2017

Accounting Standards Issued But Not Yet Adopted

The following ASUs have been issued and are expected to result in a significant change to our significant accounting policies and/or have a significant financial impact:

Credit Losses - In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326). The ASU alters the current method for recognizing credit losses within the reserve account. Currently, an institution uses the incurred loss method, the new guidance requires financial assets to be presented at the net amount expected to be collected (i.e., net of expected credit losses). The measurement of expected credit losses should be based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019. We have established an internal steering committee to lead the implementation efforts. The steering committee is in the process of evaluating control and process framework, data, model, and resource requirements and areas where modifications will be required. We are currently evaluating the impact adoption of the guidance will have on our Consolidated Financial Statements, and highlight that any impact will be contingent upon the underlying characteristics of the affected portfolio and macroeconomic and internal forecasts at adoption date.

Leases - In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842): Section A - Leases: Amendments to the FASB Accounting Standards Codification, Section B - Conforming Amendments Related to Leases: Amendment to the FASB Accounting Standards Codification, Section C - Background Information and Basis For Conclusions. Lessees will need to recognize substantially all leases on their balance sheet as a right-of-use asset and a lease liability. For income statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Classification will be based on criteria that are largely similar to those applied in current lease accounting. ASU 2016-02 is effective retrospectively for fiscal years beginning after December 15, 2018 and early adoption is permitted. The guidance in ASU 2016-02 supersedes Topic 840, Leases. Upon adoption and implementation, we expect to gross up assets and liabilities due to the recognition of lease liabilities and right of use assets associated with the underlying lease contracts. While we do not expect the adoption of the guidance to have a material impact on our Consolidated Statements of Operations given our current inventory of leases, review is ongoing and we will continue to evaluate the impact to the Consolidated Statements of Financial Condition and to capital.

Revenue from Contracts with Customers - In May 2014, FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)." Under the amended guidance, an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration in exchange for those goods or services. The FASB has voted to approve a year deferral of the effective date from January 1, 2017 to January 1, 2018. In April 2016, the FASB clarified the following two aspects: identifying performance obligations and the licensing implementation guidance, while retaining the related principles for those areas. In May 2016, the FASB issued ASU 2016-12 Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients, to provide a limited number of changes to its revenue recognition standard. The amendments clarify the assessment of the likelihood that revenue will be collected from a contract, the guidance for presenting sales taxes and similar taxes, and the timing for measuring customer payments that are not in cash. The amendment also specifies that a contract should be considered complete if all, or substantially all, of its revenue has been collected prior to making the transition to the new standard. In addition, the update clarifies the disclosure requirements for transition to the new standard by adjusting amounts from prior reporting periods. In December 2016, the FASB issued ASU 2016-20 Technical Corrections and Improvement to Topic 606, Revenue from Contracts with Customers. We expect to implement the revenue recognition guidance in the first quarter of 2018 utilizing the cumulative-effect approach. Our

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implementation of the guidance will include creation of an inventory of revenue contracts and assessing whether the recognition of revenue associated with each contract will be impacted by the new guidance, particularly related to certain fees. Lease contracts and financial instruments, which include loans and securities, are excluded from the scope of this standard. Therefore, we do not anticipate the implementation of the revenue recognition guidance to have a material impact on our Consolidated Financial Statements. The initial scoping has been completed and the amount of in scope revenue is limited, such that we do not expect implementation of the revenue recognition guidance to have a material impact on our Consolidated Financial Statements or associated disclosures.

The following ASUs have been issued and are not expected to have a material impact on our Consolidated Financial Statements and/or significant accounting policies:

Standard	Description	Effective Date
ASU 2017-11	Earnings Per Share (Topic 260); Distinguishing Liabilities from Equity (Topic 480); Derivatives and Hedging (Topic 815): (Part I) Accounting for Certain Financial Instruments with Down Round Features, (Part II) Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Non-controlling Interests with a Scope.	January 1, 2019
ASU 2017-10	Service Concession Arrangements (Topic 853): Determining the Customer of the Operation Services (a consensus of the FASB Emerging Issues Task Force)	January 1, 2018
ASU 2017-09	Update 2017-09—Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting	January 1, 2018
ASU 2017-08	Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities	January 1, 2019
ASU 2017-07	Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost	January 1, 2018
ASU 2017-06	Plan Accounting - Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): Employee Benefit Plan Master Trust Reporting	January 1, 2019
ASU 2017-05	Other Income - Gains and Losses from the De-recognition of Non-financial Assets (Subtopic 610-20): Clarifying the Scope of Asset De-recognition Guidance and Accounting for Partial Sales of Non-financial Assets	January 1, 2018
ASU 2017-04	Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment	January 1, 2020
ASU 2017-01	Business Combinations (Topic 805): Clarifying the Definition of a Business	January 1, 2018
ASU 2016-18	Statement of Cash Flows (Topic 230): Restricted Cash	January 1, 2018
ASU 2016-16	Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory	January 1, 2018
ASU 2016-15	Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments	January 1, 2018
ASU 2016-04	Liabilities - Extinguishment of Liabilities (Subtopic 504-20): Recognition of Breakage for Certain Prepaid Stored-Value Products	January 1, 2018
ASU 2016-01	Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities	January 1, 2018

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

A discussion regarding our management of market risk is included in "Market Risk" in this report in "Management's Discussion and Analysis of Financial Condition and Results of Operations" which is incorporated herein by reference.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. As of June 30, 2017, pursuant to Rule 13a-15(b) of the Securities Exchange Act of 1934, as amended ("Exchange Act"), an evaluation was performed by the Company's management, including our principal executive and financial officers, regarding the design and effectiveness of our disclosure controls and procedures. Based upon that evaluation, the principal executive and financial officers have (a) concluded that our current disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms as of June 30, 2017.

Changes in Internal Controls. There have been no changes in the Company's internal control over financial (b) reporting (as defined in Rule 13a-15(d) of the Exchange Act) during the three months ended June 30, 2017, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II

Item 1. Legal Proceedings

From time to time, the Company is party to legal proceedings incidental to its business. For further information, see Note 16 - Legal Proceedings, Contingencies and Commitments.

Item 1A. Risk Factors

The Company believes that there have been no material changes to the risk factors previously disclosed in response to Item 1A to Part I of our Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Sale of Unregistered Securities

The Company made no sales of unregistered securities during the quarter ended June 30, 2017.

Issuer Purchases of Equity Securities

The Company made no purchases of its equity securities during the quarter ended June 30, 2017.

Item 3. Defaults upon Senior Securities

The Company had no defaults on senior securities.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit No. Description

3.1	Second Amended and Restated Articles of Incorporation of Flagstar Bancorp, Inc., as amended
3.2	Sixth Amended and Restated Bylaws of the Company (previously filed as Exhibit 3.2 to the Company's Current Report on Form 10-Q, dated November 7, 2016, and incorporated herein by reference).
10.1	Flagstar Bancorp, Inc. 2016 Stock Award and Incentive Plan Restricted Stock Unit and Performance Share Unit Senior Executive Officer Form of Award Agreement
11	Statement regarding computation of per share earnings is incorporated by reference to Note 13 of the Notes to the Consolidated Financial Statements, in Item 1. Financial Statements.
31.1	Section 302 Certification of Chief Executive Officer

- 31.2 Section 302 Certification of Chief Financial Officer
- 32.1 Section 906 Certification, as furnished by the Chief Executive Officer
- 32.2 Section 906 Certification, as furnished by the Chief Financial Officer

101 Financial statements from Quarterly Report on Form 10-Q of the Company for the quarter ended June 30, 2017, formatted in XBRL: (i) the Consolidated Statements of Financial Condition, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Comprehensive Income (Loss), (iv) the Consolidated Statements of Stockholders' Equity, (v) the Consolidated Statements of Cash Flows and (vi) the Notes to the Consolidated Financial Statements.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FLAGSTAR BANCORP, INC.
Registrant

Date: August 7, 2017 /s/ Alessandro DiNello
Alessandro DiNello
President and Chief Executive Officer
(Principal Executive Officer)

/s/ James K. Cirolì
James K. Cirolì
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

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