FLUSHING FINANCIAL CORP
Form 10-K
March 17, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2007

Commission file number **000-24272**

FLUSHING FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**11-3209278**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1979 Marcus Avenue, Suite E140, Lake Success, New York 11042

(Address of principal executive offices)

(718) 961-5400

(Registrant s telephone number, including area code)

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

Common Stock $0.01 par value (and associated Preferred Stock Purchase Rights).	**NASDAQ Global Select Market**
(Title of each class)	(Name of exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: **None.**

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

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

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. x Yes o No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o	Smaller reporting company o

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

As of June 29, 2007, the last business day of the registrant s most recently completed second fiscal quarter, the aggregate market value of the voting stock held by non-affiliates of the registrant was $324,977,000. This figure is based on the closing price on that date on the NASDAQ Global Select Market for a share of the registrant s Common Stock, $0.01 par value, which was $16.06.

The number of shares of the registrant s Common Stock outstanding as of February 29, 2008 was 21,336,786 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Company s definitive Proxy Statement for the Annual Meeting of Stockholders to be held on May 20, 2008 are incorporated herein by reference in Part III.

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SIGNATURES

POWER OF ATTORNEY

CAUTIONARY NOTE REGARDING FORWARD LOOKING STATEMENTS

Statements contained in this Annual Report on Form 10-K (this Annual Report) relating to plans, strategies, economic performance and trends, projections of results of specific activities or investments and other statements that are not descriptions of historical facts may be forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking information is inherently subject to risks and uncertainties, and actual results could differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed under the captions Business General Allowance for Loan Losses and Business General Market Area and Competition in Item 1 below, Risk Factors in Item 1A below, in Managemen Discussion and Analysis of Financial Condition and Results of Operations Overview in Item 7 below, and elsewhere in this Annual Report and in other documents filed by the Company with the Securities and Exchange Commission from time to time. Forward-looking statements may be identified by terms such as may , will , should , could , expects , plans , intends , anticipates , believes , estimates , predicts , continue or similar terms or the negative of these terms. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. The Company has no obligation to update these forward-looking statements.

PART I

Item 1. Business.

GENERAL

Overview

Flushing Financial Corporation (the Holding Company) is a Delaware corporation organized in May 1994 at the direction of Flushing Savings Bank, FSB (the Bank). The Bank was organized in 1929 as a New York State chartered mutual savings bank. In 1994, the Bank converted to a federally chartered mutual savings bank and changed its name from Flushing Savings Bank to Flushing Savings Bank, FSB. The Bank converted from a federally chartered mutual savings bank to a federally chartered stock savings bank on November 21, 1995, at which time the Holding Company acquired all of the stock of the Bank. The primary business of the Holding Company at this time is the operation of its wholly owned subsidiary, the Bank. The Bank owns four subsidiaries: Flushing Commercial Bank, Flushing Preferred Funding Corporation, Flushing Service Corporation, and FSB Properties Inc. In November, 2006, the Bank launched an internet branch, iGObanking.com®. The activities of the Holding Company are primarily funded by dividends, if any, received from the Bank. Flushing Financial Corporation s common stock is traded on the NASDAQ Global Select Market under the symbol FFIC.

The Holding Company also owns Flushing Financial Capital Trust II, Flushing Financial Capital Trust III, and Flushing Financial Capital Trust IV (the Trusts), special purpose business trusts formed during 2007 to issue capital securities. The Trusts used the proceeds from the issuance of these capital securities, and the proceeds from the issuance of their common stock, to purchase junior subordinated debentures from the Holding Company. In accordance with the requirements of FASB Interpretation No. 46R, the Trusts are not included in the consolidated financial statements of the Holding Company. The Holding Company previously owned Flushing Financial Capital Trust I (the Trust), which was a special purpose business trust formed in 2002 similar to the Trusts discussed above. The Trust called its outstanding capital securities during July 2007, and was then liquidated. Prior to 2004, the Trust was included in the consolidated financial statements of the Company. Effective January 1, 2004, in accordance with the requirements of FASB Interpretation No. 46R, the Trust was deconsolidated.

Unless otherwise disclosed, the information presented in this Annual Report reflects the financial condition and results of operations of the Holding Company, the Bank and the Bank s subsidiaries on a consolidated basis (collectively, the Company). At December 31, 2007, the Company had total assets of $3.4 billion, deposits of $2.0 billion and stockholders equity of $233.7 million.

The Bank s principal business is attracting retail deposits from the general public and investing those deposits together with funds generated from ongoing operations and borrowings, primarily in (1) originations and purchases of one-to-four family (focusing on mixed-use properties properties that contain both residential dwelling units and commercial units), multi-family residential and commercial real estate mortgage loans; (2) construction loans, primarily for multi-family residential properties; (3) Small Business Administration (SBA) loans and other small business loans; (4) mortgage loan surrogates such as mortgage-backed securities; and (5) U.S. government securities, corporate fixed-

income securities and other marketable securities. The Bank also originates certain other consumer loans. The Bank s revenues are derived principally from interest on its mortgage and other loans and mortgage-backed securities portfolio, and interest and dividends on other investments in its securities portfolio. The Bank s primary sources of funds are deposits, Federal Home Loan Bank of New York (FHLB-NY) borrowings, repurchase agreements, principal and interest payments on loans, mortgage-backed and other securities, proceeds from sales of securities and, to a lesser extent, proceeds from sales of loans. As a federal savings bank, the Bank s primary regulator is the Office of Thrift Supervision (OTS). The Bank s deposits are insured to the maximum allowable amount by the Federal Deposit Insurance Corporation (FDIC). Additionally, the Bank is a member of the Federal Home Loan Bank (FHLB) system.

In addition to operating the Bank, the Holding Company invests primarily in U.S. government securities, mortgage-backed securities, and corporate securities. The Holding Company also holds a note evidencing a loan that it made to an employee benefit trust established by the Holding Company for the purpose of holding shares for allocation or distribution under certain employee benefit plans of the Holding Company and the Bank (the Employee Benefit Trust). The funds provided by this loan enabled the Employee Benefit Trust to acquire 2,328,750 shares, or 8% of the common stock issued in our initial public offering.

On June 30, 2006, the Company acquired all of the outstanding common stock of Atlantic Liberty Financial Corporation (Atlantic Liberty), the parent holding company for Atlantic Liberty Savings, F.A., based in Brooklyn, New York. The aggregate purchase price was $42.5 million, which consisted of $14.7 million of cash, common stock valued at $26.6 million, and $1.3 million assigned to the fair value of Atlantic Liberty s outstanding stock options. Under the terms of the Agreement and Plan of Merger, dated December 20, 2005, Atlantic Liberty s shareholders received $24.00 in cash, 1.43 Holding Company shares per Atlantic Liberty share owned, or a combination thereof, subject to aggregate allocation to all Atlantic Liberty s shareholders of 65% stock / 35% cash. In connection with the merger, the Company issued 1.6 million shares of common stock, the value of which was determined based on the closing price of the Company s common stock on the announcement date of December 21, 2005, and two days prior to and after the announcement date. The Company acquired $186.9 million in assets, $116.2 million in net loans and assumed $106.8 million in deposits. This acquisition provided the Bank a presence on Montague Street and on Avenue J in Brooklyn, two highly attractive markets.

During 2006, the Bank established a business banking unit. The Bank s business plan includes a transition from a traditional thrift to a more commercial like banking institution by focusing on the development of a full complement of commercial business deposit, loan and cash management products.

On November 27, 2006, the Bank launched an internet branch, iGObanking.com®, as a new division which provides the Bank access to markets outside its geographic locations. Accounts can be opened online at www.iGObanking.com or by mail.

During 2007, the Bank formed a wholly owned subsidiary, Flushing Commercial Bank, a New York State chartered commercial bank, for the limited purpose of accepting municipal deposits and state funds, including certain court ordered funds from New York State Courts, in the State of New York. The commercial bank was formed in response to a New York State Finance Law which requires that municipal deposits and state funds must be deposited into a bank or trust company designated by the New York State Comptroller. The Bank is not considered a bank or trust company for this purpose. The commercial bank offers a full range of deposit products to municipalities and New York State, similar to the products currently being offered by the Bank, but does not make loans. To date, the operations of Flushing Commercial Bank have not been material.

Market Area and Competition

The Bank is a community oriented savings institution offering a wide variety of financial services to meet the needs of the communities it serves. The Bank s main office is in Flushing, New York, located in the Borough of Queens. At December 31, 2007, the Bank operated out of its main office and thirteen branch offices, located in the New York City Boroughs of Queens, Brooklyn, and Manhattan, and in Nassau County, New York. The Bank also operates an internet branch, iGObanking.com®. The Bank maintains its executive offices in Lake Success in Nassau County, New York. Substantially all of the Bank s mortgage loans are secured by properties located in the New York City metropolitan area. During the last three years, real estate values in the New York City metropolitan area have been stable, which has favorably impacted the Bank s asset quality. See Asset Quality and Risk Factors Local Economic Conditions included in Item 1A of this Annual Report. There can be no assurance that the stability of these economic factors will continue.

The Bank faces intense and increasing competition both in making loans and in attracting deposits. The Bank s market area has a high density of financial institutions, many of which have greater financial resources, name recognition and market presence than the Bank, and all of which are competitors of the Bank to varying degrees. Particularly intense competition exists for deposits and in all of the lending activities emphasized by the Bank. The internet banking arena, which the Bank entered in November 2006, also has many larger financial institutions which have greater financial resources, name recognition and market presence than the Bank. The future earnings prospects of the Bank will be affected by the Bank s ability to compete effectively with other financial institutions and to implement its business strategies. See Risk Factors The Markets in Which the Bank Operates Are Highly Competitive included in Item 1A of this Annual Report.

For a discussion of the Company s business strategies, see Management s Discussion and Analysis of Financial Condition and Results of Operations Overview Management Strategy included in Item 7 of this Annual Report.

Lending Activities

Loan Portfolio Composition. The Bank s loan portfolio consists primarily of mortgage loans secured by multi-family residential, commercial real estate, one-to-four family mixed-use property, one-to-four family residential property, and construction loans. In addition, the Bank also offers SBA loans, other small business loans and consumer loans. Substantially all the Bank s mortgage loans are secured by properties located within the Bank s market area. At December 31, 2007, the Bank had gross loans outstanding of $2,694.7 million (before the allowance for loan losses and net deferred costs).

Beginning in late 2001, the Bank shifted its focus from originating one-to-four family residential property mortgage loans to the origination of multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loans. These loans generally have higher yields than one-to-four family residential properties, and include prepayment penalties that the Bank collects if the loans pay in full prior to the contractual maturity. From December 31, 2001 to December 31, 2007, multi-family residential mortgage loans increased $594.8 million, or 160.9%, commercial real estate mortgage loans increased $411.4 million, or 191.9%, one-to-four family mixed-use property mortgage loans increased $577.1 million, or 525.6%, while one-to-four family residential property mortgage loans decreased $190.3 million, or 54.1%. The Bank expects to continue this emphasis through marketing and by maintaining competitive interest rates and origination fees. The Bank s marketing efforts include frequent contacts with mortgage brokers and other professionals who serve as referral sources. From time-to-time, the Bank may purchase loans from mortgage bankers and other financial institutions. Loans purchased comply with the Bank s underwriting standards.

Fully underwritten one-to-four family residential mortgage loans generally are considered by the banking industry to have less risk than other types of loans. Multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loans generally have higher yields than one-to-four family residential property mortgage loans and shorter terms to maturity, but typically involve higher principal amounts and generally expose the lender to a greater risk of credit loss than one-to-four family residential property mortgage loans. The Bank s increased emphasis on multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loans has increased the overall level of credit risk inherent in the Bank s loan portfolio. The greater risk associated with multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loans could require the Bank to increase its provision for loan losses and to maintain an allowance for loan losses as a percentage of total loans in excess of the allowance currently maintained by the Bank. To date, the Bank has not experienced significant losses in its multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loan portfolios, and has determined that, at this time, additional provisions are not required.

The Bank s mortgage loan portfolio consists of adjustable rate mortgage (ARM) loans and fixed-rate mortgage loans. Interest rates charged by the Bank on loans are affected primarily by the demand for such loans, the supply of money available for lending purposes, the rate offered by the Bank s competitors and the creditworthiness of the borrower. Many of those factors are, in turn, affected by regional and national economic conditions, and the fiscal, monetary and tax policies of the federal government.

In general, consumers show a preference for ARM loans in periods of high interest rates and for fixed-rate loans when interest rates are low. In periods of declining interest rates, the Bank may experience refinancing activity in ARM loans, as borrowers show a preference to lock-in the lower rates available on fixed-rate loans. In the case of ARM loans originated by the Bank, volume and adjustment periods are affected by the interest rates and other market factors as

discussed above as well as consumer preferences. The Bank has not in the past, nor does it currently, originate ARM loans that provide for negative amortization.

In recent years, the Bank has grown its construction loan portfolio. The Bank obtains a first lien position on the underlying collateral, and generally obtains personal guarantees on construction loans. These loans generally have a term of two years or less. Construction loans involve a greater degree of risk than other loans because, among other things, the underwriting of such loans is based on an estimated value of the developed property, which can be difficult to ascertain in light of uncertainties inherent in such estimations. In addition, construction lending entails the risk that the project may not be completed due to cost overruns or changes in market conditions. The greater risk associated with construction loans could require the Bank to increase its provision for loan losses, and to maintain an allowance for loan losses as a percentage of total loans in excess of the allowance currently maintained by the Bank. To date, the Bank has not incurred significant losses in its construction loan portfolio.

The business banking unit was formed in 2006 to focus on loans to businesses located within the Bank s market area. These loans are generally personally guaranteed by the owners, and may be secured by the assets of the business. The interest rate on these loans is generally an adjustable rate based on a published index, usually the prime rate. These loans, while providing a higher rate of return to the Bank, also present a higher level of risk. The greater risk associated with business loans could require the Bank to increase its provision for loan losses, and to maintain an allowance for loan losses as a percentage of total loans in excess of the allowance currently maintained by the Bank. To date, the Bank has not incurred significant losses in its business loan portfolio.

The Bank s lending activities are subject to federal and state laws and regulations. See Regulation.

The following table sets forth the composition of the Bank s loan portfolio at the dates indicated.

	At December 31,									
	2007		2006		2005		2004		2003	
	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total
	(Dollars in thousands)									
Mortgage Loans:										
Multi-family residential	$ 964,455	35.79%	$ 870,912	37.52%	$ 788,071	41.92%	$ 646,922	42.61%	$ 541,837	42.53%
Commercial real estate	625,843	23.23	519,552	22.38	399,081	21.23	334,048	22.00	290,332	22.79
One-to-four family - mixed-use property	686,921	25.49	588,092	25.33	477,775	25.42	332,805	21.92	226,225	17.76
One-to-four family - residential (1)	161,666	6.01	161,889	6.98	134,641	7.17	151,737	10.00	178,474	14.01
Co-operative apartment (2)	7,070	0.26	8,059	0.35	2,161	0.11	3,132	0.21	3,729	0.29
Construction	119,745	4.44	104,488	4.50	49,522	2.63	31,460	2.07	23,622	1.85
Gross mortgage loans	2,565,700	95.22	2,252,992	97.06	1,851,251	98.48	1,500,104	98.81	1,264,219	99.23
Small Business Administration loans	18,922	0.70	17,521	0.75	9,239	0.49	5,633	0.37	4,931	0.39
Commercial business and other loans	110,046	4.08	50,899	2.19	19,362	1.03	12,505	0.82	4,894	0.38
Gross loans	2,694,668	100.00%	2,321,412	100.00%	1,879,852	100.00%	1,518,242	100.00%	1,274,044	100.00%
Unearned loan fees and deferred costs, net	14,083		10,393		8,409		4,798		2,030	
Less: Allowance for loan losses	(6,633)		(7,057)		(6,385)		(6,533)		(6,553)	
Loans, net	$ 2,702,118		$ 2,324,748		$ 1,881,876		$ 1,516,507		$ 1,269,521	

(1) One-to-four family residential mortgage loans also include home equity and condominium loans. At December 31, 2007, gross home equity loans totaled $36.1 million and condominium loans totaled $8.7 million.

(2) Consists of loans secured by shares representing interests in individual co-operative units that are generally owner occupied.

The following table sets forth the Bank s loan originations (including the net effect of refinancings) and the changes in the Bank s portfolio of loans, including purchases, sales and principal reductions for the years indicated:

(In thousands)	For the years ended December 31, 2007	2006	2005
Mortgage Loans			
At beginning of year	$ 2,252,992	$ 1,851,251	$ 1,500,104
Mortgage loans originated:			
Multi-family residential	222,625	166,744	222,065
Commercial real estate	165,440	150,804	103,090
One-to-four family mixed-use property	159,331	154,456	186,700
One-to-four family residential	36,397	13,786	13,186
Co-operative apartment	828	125	
Construction	54,151	73,107	46,414
Total mortgage loans originated	638,772	559,022	571,455
Mortgage loans purchased:			
Multi-family residential	8,717		1,009
Commercial real estate	2,902	3,087	
Construction		1,980	
Acquisition of Atlantic Liberty loans:			
Multi-family residential		16,299	
Commercial real estate		31,914	
One-to-four family mixed-use property		9,333	
One-to-four family residential		51,033	
Co-operative apartment		6,665	
Construction		13,781	
Total mortgage loans purchased/acquired	11,619	134,092	1,009
Less:			
Principal reductions	284,608	270,416	217,199
Mortgage loan sales	53,075	20,957	4,118
Mortgage loan foreclosures			
At end of year	$ 2,565,700	$ 2,252,992	$ 1,851,251
SBA, Commercial Business & Other Loans			
At beginning of year	$ 68,420	$ 28,601	$ 18,138
Loans originated:			
SBA loans	12,840	19,914	12,249
Small business loans (1)	92,240	49,909	12,410
Other loans	1,953	1,671	1,537
Total other loans originated	107,033	71,494	26,196
Less:			
Sales	4,925	7,477	6,630

Repayments (1)	41,090	24,116	8,940
Charge-offs	470	82	163
At end of year	$ 128,968	$ 68,420	$ 28,601

1) 2006 includes an $11.5 million loan to Atlantic Liberty prior to the merger.

Loan Maturity and Repricing. The following table shows the maturity of the Bank s commercial mortgage loan, construction loan and non-mortgage loan portfolios at December 31, 2007. Scheduled repayments are shown in the maturity category in which the payments become due.

(In thousands)	Commercial Mortgage Loans	Construction	SBA	Commercial Business and Other	Total
Amounts due within one year	$ 68,505	$ 98,282	$ 7,729	$ 54,692	$ 229,208
Amounts due after one year:					
One to two years	60,932	16,396	1,992	31,701	111,021
Two to three years	51,594	5,067	1,929	13,806	72,396
Three to five years	106,524		3,163	6,128	115,815
Over five years	338,288		4,109	3,719	346,116
Total due after one year	557,338	21,463	11,193	55,354	645,348
Total amounts due	$ 625,843	$ 119,745	$ 18,922	$ 110,046	$ 874,556
Sensitivity of loans to changes in interest rates - loans due after one year:					
Fixed rate loans	$ 118,998	$ 10,570	$ 116	$ 45,273	$ 174,957
Adjustable rate loans	438,340	10,893	11,077	10,081	470,391
Total loans due after one year	$ 557,338	$ 21,463	$ 11,193	$ 55,354	$ 645,348

Multi-Family Residential Lending. Loans secured by multi-family residential properties were $964.5 million, or 35.79% of gross loans, at December 31, 2007. The Bank s multi-family residential mortgage loans had an average principal balance of $497,000 at December 31, 2007, and the largest multi-family residential mortgage loan held in the Bank s portfolio had a principal balance of $11.2 million. The Bank offers both fixed-rate and adjustable rate multi-family residential mortgage loans, with maturities up to 30 years.

In underwriting multi-family residential mortgage loans, the Bank reviews the expected net operating income generated by the real estate collateral securing the loan, the age and condition of the collateral, the financial resources and income level of the borrower and the borrower s experience in owning or managing similar properties. The Bank typically requires debt service coverage of at least 125% of the monthly loan payment. The Bank generally originates these loans up to only 75% of the appraised value or the purchase price of the property, whichever is less. Any loan with a final loan-to-value ratio in excess of 75% must be approved by either the Board of Directors or its Executive Committee as an exception to policy. The Bank generally relies on the income generated by the property as the primary means by which the loan is repaid. However, personal guarantees may be obtained for additional security from these borrowers. The Bank typically orders an environmental report on its multifamily and commercial real estate loans.

Loans secured by multi-family residential property generally involve a greater degree of risk than residential mortgage loans and carry larger loan balances. The increased credit risk is a result of several factors, including the concentration of principal in a smaller number of loans and borrowers, the effects of general economic conditions on income producing properties and the increased difficulty in evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by multi-family residential property is typically dependent upon the successful operation of the related property. If the cash flow from the property is reduced, the borrower s ability to repay the loan may be impaired. Loans secured by multi-family residential property also may involve a greater degree of environmental risk. The Bank seeks to protect against this risk through obtaining an environmental report. See Asset Quality Real Estate Owned.

The Bank s fixed-rate multi-family mortgage loans are originated for terms up to 15 years and are competitively priced based on market conditions and the Bank s cost of funds. The Bank originated and purchased $72.1 million, $47.0 million and $44.3 million of fixed-rate multi-family mortgage loans in 2007, 2006 and 2005, respectively. At December 31, 2007, $244.8 million, or 25.4%, of the Bank s multi-family mortgage loans consisted of fixed rate loans.

The Bank offers ARM loans with adjustment periods typically of five years and for terms of up to 30 years. Interest rates on ARM loans currently offered by the Bank are adjusted at the beginning of each adjustment period based upon a fixed spread above the FHLB-NY corresponding Regular Advance Rate. From time to time, the Bank may

originate ARM loans at an initial rate lower than the index as a result of a discount on the spread for the initial adjustment period. Multi-family adjustable-rate mortgage loans generally are not subject to limitations on interest rate increases either on an adjustment period or aggregate basis over the life of the loan. The Bank originated and purchased multi-family ARM loans totaling $159.3 million, $119.8 million and $178.8 million during 2007, 2006 and 2005, respectively. At December 31, 2007, $719.6 million, or 74.6%, of the Bank s multi-family mortgage loans consisted of ARM loans.

Commercial Real Estate Lending. Loans secured by commercial real estate were $625.8 million, or 23.23% of the Bank s gross loans, at December 31, 2007. The Bank s commercial real estate mortgage loans are secured by improved properties such as office buildings, hotels/motels, nursing homes, small business facilities, strip shopping centers, warehouses, and, to a lesser extent, religious facilities. At December 31, 2007, the Bank s commercial real estate mortgage loans had an average principal balance of $778,000, and the largest of such loans, which was secured by a multi-tenant shopping center, had a principal balance of $11.5 million. Commercial real estate mortgage loans are generally originated in a range of $100,000 to $6.0 million. Commercial real estate mortgage loans are generally offered at adjustable rates tied to a market index for terms of five to 15 years, with adjustment periods from one to five years. Commercial real estate mortgage loans are also made at fixed interest rates for terms of seven, 10 or 15 years.

In underwriting commercial real estate mortgage loans, the Bank employs the same underwriting standards and procedures as are employed in underwriting multi-family residential mortgage loans.

Commercial real estate mortgage loans generally carry larger loan balances than one-to-four family residential mortgage loans and involve a greater degree of credit risk for the same reasons applicable to multi-family loans.

The Bank s fixed-rate commercial mortgage loans are originated for terms up to 20 years and are competitively priced based on market conditions and the Bank s cost of funds. The Bank originated and purchased $28.4 million, $20.5 million and $17.7 million of fixed-rate commercial mortgage loans in 2007, 2006 and 2005, respectively. At December 31, 2007, $149.8 million, or 23.9%, of the Bank s commercial mortgage loans consisted of fixed rate loans.

The Bank offers ARM loans with adjustment periods of one to five years and for terms of up to 15 years. Interest rates on ARM loans currently offered by the Bank are adjusted at the beginning of each adjustment period based upon a fixed spread above the FHLB-NY corresponding Regular Advance Rate. From time to time, the Bank may originate ARM loans at an initial rate lower than the index as a result of a discount on the spread for the initial adjustment period. Commercial adjustable-rate mortgage loans generally are not subject to limitations on interest rate increases either on an adjustment period or aggregate basis over the life of the loan. The Bank originated and purchased commercial ARM loans totaling $140.0 million, $133.4 million and $85.4 million during 2007, 2006 and 2005, respectively. At December 31, 2007, $476.1 million, or 76.1%, of the Bank s commercial mortgage loans consisted of ARM loans.

One-to-Four Family Mortgage Lending Mixed-Use Properties. The Bank offers mortgage loans secured by one-to-four family mixed-use properties. These properties contain up to four residential dwelling units and a commercial unit. The Bank offers both fixed-rate and adjustable-rate one-to-four family mixed-use property mortgage loans with maturities of up to 30 years and a general maximum loan amount of $1,000,000. Loan originations primarily result from applications received from mortgage brokers and mortgage bankers, existing or past customers, and persons who respond to Bank marketing efforts and referrals. One-to-four family mixed-use property mortgage loans were $686.9 million, or 25.49% of gross loans, at December 31, 2007.

During the three-year period ended December 31, 2007, the Bank focused its origination efforts with respect to one-to-four family mortgage loans on mixed-use properties. The primary income-producing units of these properties are the residential dwelling units. One-to-four family mixed-use property mortgage loans generally have a higher interest rate than residential mortgage loans. One-to-four family mixed-use property mortgage loans also have a higher degree of risk than residential mortgage loans, as repayment of the loan is usually dependent on the income produced from renting the residential units and the commercial unit. At December 31, 2007, one-to-four family mixed-use property mortgage loans amounted to $686.9 million, as compared to $588.1 million at December 31, 2006, $477.8 million at December 31, 2005, and $332.8 million at December 31, 2004, representing an increase of $354.1 million during the three-year period.

In underwriting one-to-four family mixed-use property mortgage loans, the Bank employs the same underwriting standards as are employed in underwriting multi-family residential mortgage loans.

The Bank s fixed-rate one-to-four family mixed-use property mortgage loans are originated for terms of up to 30 years and are competitively priced based on market conditions and the Bank s cost of funds. The Bank originated and purchased $33.7 million, $30.8 million and $39.4 million of fixed-rate one-to-four family mixed-use property mortgage

loans in 2007, 2006 and 2005, respectively. At December 31, 2007, $171.2 million, or 24.9%, of the Bank s one-to-four family mixed-use property mortgage loans consisted of fixed rate loans.

The Bank offers adjustable-rate one-to-four family mixed-use property mortgage loans with adjustment periods typically of five years and for terms of up to 30 years. Interest rates on ARM loans currently offered by the Bank are adjusted at the beginning of each adjustment period based upon a fixed spread above the FHLB-NY corresponding Regular Advance Rate. From time to time, the Bank may originate ARM loans at an initial rate lower than the index as a result of a discount on the spread for the initial adjustment period. One-to-four family mixed-use property adjustable-rate mortgage loans generally are not subject to limitations on interest rate increases either on an adjustment period or aggregate basis over the life of the loan. The Bank originated and purchased one-to-four family mixed-use property ARM loans totaling $125.7 million, $123.7 million and $147.3 million during 2007, 2006 and 2005, respectively. At December 31, 2007, $515.7 million, or 75.1%, of the Bank s one-to-four family mixed-use property mortgage loans consisted of ARM loans.

One-to-Four Family Mortgage Lending Residential Properties. The Bank offers mortgage loans secured by one-to-four family residential properties, including townhouses and condominium units. For purposes of the description contained in this section, one-to-four family residential mortgage loans, co-operative apartment loans and home equity loans are collectively referred to herein as residential mortgage loans. The Bank offers both fixed-rate and adjustable-rate residential mortgage loans with maturities of up to 30 years and a general maximum loan amount of $750,000. Loan originations generally result from applications received from mortgage brokers and mortgage bankers, existing or past customers, and referrals. Residential mortgage loans were $168.7 million, or 6.27% of gross loans, at December 31, 2007.

The Bank generally originates residential mortgage loans in amounts up to 80% of the appraised value or the sale price, whichever is less. The Bank may make residential mortgage loans with loan-to-value ratios of up to 90% of the appraised value of the mortgaged property; however, private mortgage insurance is required whenever loan-to-value ratios exceed 80% of the appraised value of the property securing the loan.

The Bank originates residential mortgage loans to self-employed individuals within the Bank s local community without verification of the borrower s level of income, provided that the borrower s stated income is considered reasonable for the borrower s type of business. These loans involve a higher degree of risk as compared to the Bank s other fully underwritten residential mortgage loans as there is a greater opportunity for self-employed borrowers to falsify or overstate their level of income and ability to service indebtedness. This risk is mitigated by the Bank s policy to limit the amount of one-to-four family residential mortgage loans to 80% of the appraised value of the property or the sale price, whichever is less. The Bank believes that its willingness to make such loans is an aspect of its commitment to be a community-oriented bank. The Bank originated $2.4 million and $0.9 million of these first mortgage loans during 2007 and 2006, respectively. The Bank did not originate any of these loans during 2005. The Bank also extended $43.0 million in home equity lines of credit during 2007 without verification of the borrower s level of income.

The Bank s fixed-rate residential mortgage loans typically are originated for terms of 15 and 30 years and are competitively priced based on market conditions and the Bank s cost of funds. The Bank did not originate or purchase any 15-year fixed-rate residential mortgages in 2007. The Bank originated and purchased $0.4 million and $0.1 million of 15-year fixed-rate residential mortgage loans in 2006 and 2005, respectively. The Bank originated $0.5 million of 30-year fixed-rate mortgages in 2007. The Bank did not originate or purchase any 30-year fixed rate residential mortgages in 2006 and 2005. These loans have been retained to provide flexibility in the management of the Company s interest rate sensitivity position. At December 31, 2007, $70.8 million, or 41.9%, of the Bank s residential mortgage loans consisted of fixed rate loans.

The Bank offers ARM loans with adjustment periods of one, three, five, seven or ten years. Interest rates on ARM loans currently offered by the Bank are adjusted at the beginning of each adjustment period based upon a fixed spread above the average yield on United States treasury securities, adjusted to the U.S. Treasury constant maturity index as published weekly by the Federal Reserve Board. From time to time, the Bank may originate ARM loans at an initial rate lower than the U.S. Treasury constant maturity index as a result of a discount on the spread for the initial adjustment period. ARM loans generally are subject to limitations on interest rate increases of 2% per adjustment period and an aggregate adjustment of 6% over the life of the loan. The Bank originated and purchased adjustable rate residential mortgage loans totaling $36.8 million, $13.5 million and $13.1 million during 2007, 2006 and 2005, respectively. At December 31, 2007, $98.0 million, or 58.1%, of the Bank s residential mortgage loans consisted of ARM loans.

The retention of ARM loans in the Bank s portfolio helps reduce the Bank s exposure to interest rate risks. However, in an environment of rapidly increasing interest rates, it is possible for the interest rate increase to exceed the

maximum aggregate adjustment on one-to-four family residential ARM loans and negatively affect the spread between the Bank s interest income and its cost of funds.

ARM loans generally involve credit risks different from those inherent in fixed-rate loans, primarily because if interest rates rise, the underlying payments of the borrower rise, thereby increasing the potential for default. However, this potential risk is lessened by the Bank s policy of originating one-to-four family residential ARM loans with annual and lifetime interest rate caps that limit the increase of a borrower s monthly payment.

Home equity loans are included in the Bank s portfolio of residential mortgage loans. These loans are offered as adjustable-rate home equity lines of credit on which interest only is due for an initial term of 10 years and thereafter principal and interest payments sufficient to liquidate the loan are required for the remaining term, not to exceed 30 years. These loans also may be offered as fully amortizing closed-end fixed-rate loans for terms up to 15 years. All home equity loans are made on one-to-four family residential and condominium units, which are owner-occupied, and one-to-four family mixed-use properties, and are subject to an 80% loan-to-value ratio computed on the basis of the aggregate of the first mortgage loan amount outstanding and the proposed home equity loan. They are generally granted in amounts from $25,000 to $300,000. The underwriting standards for home equity loans are substantially the same as those for residential mortgage loans. At December 31, 2007, home equity loans totaled $36.1 million, or 1.34%, of gross loans.

Construction Loans. The Bank s construction loans primarily have been made to finance the construction of one-to-four family residential properties, multi-family residential properties and residential condominiums. The Bank also, to a limited extent, finances the construction of commercial real estate. The Bank s policies provide that construction loans may be made in amounts up to 70% of the estimated value of the developed property and only if the Bank obtains a first lien position on the underlying real estate. In addition, the Bank generally requires personal guarantees on all construction loans. Construction loans are generally made with terms of two years or less. Advances are made as construction progresses and inspection warrants, subject to continued title searches to ensure that the Bank maintains a first lien position. The Bank made advances on construction loans of $54.2 million, $75.1 million and $46.4 million during 2007, 2006 and 2005, respectively. Construction loans outstanding at December 31, 2007 totaled $119.7 million, or 4.44%, of gross loans.

Construction loans involve a greater degree of risk than other loans because, among other things, the underwriting of such loans is based on an estimated value of the developed property, which can be difficult to ascertain in light of uncertainties inherent in such estimations. In addition, construction lending entails the risk that the project may not be completed due to cost overruns or changes in market conditions.

Small Business Administration Lending. These loans are extended to small businesses and are guaranteed by the SBA up to a maximum of 85% of the loan balance for loans with balances of $150,000 or less, and to a maximum of 75% of the loan balance for loans with balances greater than $150,000. The Bank also provides term loans and lines of credit up to $350,000 under the SBA Express Program, on which the SBA provides a 50% guaranty. The maximum amount the SBA can guarantee is $2,000,000. All SBA loans are underwritten in accordance with SBA Standard Operating Procedures and the Bank generally obtains personal guarantees and collateral, where applicable, from SBA borrowers. Typically, SBA loans are originated at a range of $25,000 to $2.0 million with terms ranging from three to 25 years. SBA loans are generally offered at adjustable rates tied to the prime rate (as published in the Wall Street Journal) with adjustment periods of one to three months. The Bank generally sells the guaranteed portion of certain SBA term loans in the secondary market and retains the servicing rights on these loans, collecting a servicing fee of approximately 1%. The Bank originated $12.8 million, $19.9 million, and $12.2 million of SBA loans during 2007, 2006, and 2005, respectively. At December 31, 2007, SBA loans totaled $18.9 million, representing 0.70% of gross loans.

Commercial Business and Other Lending. The Bank originates other loans for business, personal, or household purposes. Total commercial business and other loans outstanding at December 31, 2007 amounted to $110.0 million, or 4.08% of gross loans. Business loans are personally guaranteed by the owners, and may also be secured by additional collateral, including equipment and inventory. Included in commercial business loans are loans made to owners of New York City taxi medallions. These loans, which totaled $68.2 million at December 31, 2007, are secured through liens on the taxi medallions. The Bank originates taxi medallion loans up to 75% of the value of the taxi medallion. The maximum loan size for a business loan is $5,000,000, with a maximum term of 25 years. The Bank originated $92.2 million, $49.9 million, and $12.4 million of commercial business loans during 2007, 2006, and 2005 respectively. Consumer loans generally consist of passbook loans and overdraft lines of credit. Generally, unsecured consumer loans are limited to amounts of $5,000 or less for terms of up to five years. The Bank offers credit cards to its customers

through a third party financial institution and receives an origination fee and transactional fees for processing such accounts, but does not underwrite or finance any portion of the credit card receivables.

The underwriting standards employed by the Bank for consumer and other loans include a determination of the applicant s payment history on other debts and assessment of the applicant s ability to meet payments on all of his or her obligations. In addition to the creditworthiness of the applicant, the underwriting process also includes a comparison of the value of the collateral, if any, to the proposed loan amount. Unsecured loans tend to have higher risk, and therefore command a higher interest rate.

Loan Approval Procedures and Authority. The Bank s Board of Directors-approved lending policies establish loan approval requirements for its various types of loan products. The Bank s Residential Mortgage Lending Policy (which applies to all one-to-four family mortgage loans, including residential and mixed-use property) establishes authorized levels of approval. One-to-four family mortgage loans that do not exceed $750,000 require two signatures for approval, one of which must be from the President, Executive Vice President or a Senior Vice President (collectively, Authorized Officers) and the other from a Senior Underwriter, Manager, Underwriter or Junior Underwriter in the Residential Mortgage Loan Department (collectively, Loan Officers). For one-to-four family mortgage loans from $750,000 to $1,000,000, three signatures are required for approval, at least two of which must be from the Authorized Officers, and the other one may be a Loan Officer. The Loan Committee, the Executive Committee or the full Board of Directors also must approve one-to-four family mortgage loans in excess of $1,000,000. Pursuant to the Bank s Commercial Real Estate Lending Policy, all loans secured by commercial real estate and multi-family residential properties, must be approved by the President or the Executive Vice President upon the recommendation of the Commercial Loan Department Officer. Such loans in excess of $1,000,000 also require Loan or Executive Committee or Board approval. In accordance with the Bank s Business Loan Policy, all business and SBA loans up to $1,000,000, and commercial and industrial loans/professional mortgage loans up to $1,500,000 must be approved by the Business Loan Committee, and ratified by the Management Loan Committee. Business and SBA loans in excess of $1,000,000 up to $2,000,000 must be approved by the Management Loan Committee and ratified by the Loan Committee of the Bank s Board of Directors. Commercial business and other loans require two signatures for approval, one of which must be from an Authorized Officer. The Bank s Construction Loan Policy requires that the Loan Committee or the Board of Directors of the Bank must approve all construction loans. Any loan, regardless of type, that deviates from the Bank s written loan policies must be approved by the Loan Committee or the Bank s Board of Directors.

For all loans originated by the Bank, upon receipt of a completed loan application, a credit report is ordered and certain other financial information is obtained. An appraisal of the real estate intended to secure the proposed loan is required. An independent appraiser designated and approved by the Bank currently performs such appraisals. The Bank s staff appraiser reviews the appraisals. The Bank s Board of Directors annually approves the independent appraisers used by the Bank and approves the Bank s appraisal policy. It is the Bank s policy to require borrowers to obtain title insurance and hazard insurance on all real estate first mortgage loans prior to closing. Borrowers generally are required to advance funds on a monthly basis together with each payment of principal and interest to a mortgage escrow account from which the Bank makes disbursements for items such as real estate taxes and, in some cases, hazard insurance premiums.

Loan Concentrations. The maximum amount of credit that the Bank can extend to any single borrower or related group of borrowers generally is limited to 15% of the Bank s unimpaired capital and surplus. Applicable law and regulations permit an additional amount of credit to be extended, equal to 10% of unimpaired capital and surplus, if the loan is secured by readily marketable collateral, which generally does not include real estate. See Regulation. However, it is currently the Bank s policy not to extend such additional credit. At December 31, 2007, the Bank had no loans in excess of the maximum dollar amount of loans to one borrower that the Bank was authorized to make. At that date, the three largest concentrations of loans to one borrower consisted of loans secured by a combination of commercial real estate and multi-family income producing properties with an aggregate principal balance of $30.4 million, $28.0 million and $23.0 million for each of the three borrowers, respectively.

Loan Servicing. At December 31, 2007, the Bank was servicing $32.0 million of mortgage loans and $17.0 million of SBA loans for others. The Bank s policy is to retain the servicing rights to the mortgage and SBA loans that it sells in the secondary market. In order to increase revenue, management intends to continue this policy.

Asset Quality

Loan Collection. When a borrower fails to make a required payment on a loan, the Bank takes a number of steps to induce the borrower to cure the delinquency and restore the loan to current status.

In the case of mortgage loans, personal contact is made with the borrower after the loan becomes 30 days delinquent. At that time, the Bank attempts to make arrangements with the borrower to either bring the loan to current status or begin making payments according to an agreed upon schedule. For the majority of delinquent loans, the borrower is able to bring the loan current within a reasonable time. When the borrower has indicated that he/she will be unable to bring the loan current, or due to other circumstances which, in management s opinion, indicate the borrower will be unable to bring the loan current within a reasonable time, or if the collateral value is deemed to have been impaired, the loan is classified as non-performing. All loans classified as non-performing, which includes all loans past due ninety days or more, are classified as non-accrual unless there is, in management s opinion, compelling evidence the borrower will bring the loan current in the immediate future. At December 31, 2007, there was one loan past due 90 days or more and still accruing interest.

Each non-performing loan is reviewed on an individual basis. Upon classifying a loan as non-performing, management reviews available information and conditions that relate to the status of the loan, including the estimated value of the loan s collateral and any legal considerations that may affect the borrower s ability to continue to make payments to the Bank. Based upon the available information, management will consider the sale of the loan or retention of the loan. If the loan is retained, the Bank may continue to work with the borrower to collect the amounts due or start foreclosure proceedings. If a foreclosure action is initiated and the loan is not brought current, paid in full, or refinanced before the foreclosure sale, the real property securing the loan generally is sold at foreclosure or by the Bank as soon thereafter as practicable.

Once the decision to sell a loan is made, management determines what would be considered adequate consideration to be obtained when that loan is sold, based on the facts and circumstances related to that loan. Investors and brokers are then contacted to seek interest in purchasing the loan. The Bank has been successful in finding buyers for its non-performing loans offered for sale that are willing to pay what it considers to be adequate consideration. Terms of the sale include cash due upon closing of the sale, no contingencies or recourse to the Bank, servicing is released to the buyer and time is of the essence. These sales usually close within a reasonably short time period.

This strategy of selling non-performing loans was implemented during 2003. This has allowed the Bank to optimize its return by quickly converting its non-performing loans to cash, which can then be reinvested in earning assets. This strategy also allows the Bank to avoid lengthy and costly legal proceedings that may occur with non-performing loans. The Bank sold forty-five delinquent mortgage loans totaling $33.9 million, thirty-five delinquent mortgage loans totaling $12.2 million, and eleven delinquent mortgage loans totaling $3.1 million during the years ended December 31, 2007, 2006 and 2005, respectively. The Bank did not record any charges to the allowance for loan losses for the non-performing loans which were sold. The Bank realized gross gains of $332,000 and no gross losses on the sale of these mortgage loans for the year ended December 31, 2007. The Bank realized gross gains of $169,000 and gross losses of $14,000 on the sale of these mortgage loans for the year ended December 31, 2006. The Bank did not realize any gross gains or losses on the sale of these mortgage loans for the year ended December 31, 2005. There can be no assurances that the Bank will continue this strategy in future periods, or if continued, it will be able to find buyers to pay adequate consideration.

On mortgage loans or loan participations purchased by the Bank, for which the seller retains the servicing rights, the Bank receives monthly reports with which it monitors the loan portfolio. Based upon servicing agreements with the servicers of the loans, the Bank relies upon the servicer to contact delinquent borrowers, collect delinquent amounts and initiate foreclosure proceedings, when necessary, all in accordance with applicable laws, regulations and the terms of the servicing agreements between the Bank and its servicing agents. At December 31, 2007, the Bank held $12.2 million of loans that were serviced by others.

In the case of commercial business or other loans, the Bank generally sends the borrower a written notice of non-payment when the loan is first past due. In the event payment is not then received, additional letters and phone calls generally are made in order to encourage the borrower to meet with a representative of the Bank to discuss the delinquency. If the loan still is not brought current and it becomes necessary for the Bank to take legal action, which typically occurs after a loan is delinquent 90 days or more, the Bank may attempt to repossess personal or business property that secures an SBA loan, commercial business loan or consumer loan.

Delinquent Loans and Non-performing Assets. The Bank generally discontinues accruing interest on delinquent loans when a loan is 90 days past due or foreclosure proceedings have been commenced, whichever first occurs. At that time, previously accrued but uncollected interest is reversed from income. Loans in default 90 days or more as to their maturity date but not their payments, however, continue to accrue interest as long as the borrower continues to remit monthly payments.

The following table sets forth information regarding all non-accrual loans and loans which are past due 90 days or more and still accruing, at the dates indicated. During the years ended December 31, 2007, 2006 and 2005, the amounts of additional interest income that would have been recorded on non-accrual loans, had they been current, totaled $256,000, $144,000 and $103,000, respectively. These amounts were not included in the Bank s interest income for the respective periods.

	At December 31,				
(Dollars in thousands)	2007	2006	2005	2004	2003
Non-accrual loans:					
Multi-family residential	$2,477	$1,957	$ 861	$	$
Commercial real estate	90	349			
One-to-four family mixed-use property					
One-to-four family residential	2,204	608	960	659	525
Co-operative apartment					
Construction					
Total non-accrual mortgage loans	4,771	2,914	1,821	659	525
Other non-accrual loans	369	212	101	252	157
Total non-accrual loans	5,140	3,126	1,922	911	682
Loans 90 days or more delinquent and still accruing	753		530		
Total non-performing loans	5,893	3,126	2,452	911	682
Foreclosed real estate					
Investment securities					
Total non-performing assets	$5,893	$3,126	$2,452	$ 911	$ 682
Troubled debt restructurings	$	$	$	$	$
Non-performing loans to gross loans	0.22%	0.13%	0.13%	0.06%	0.05%
Non-performing assets to total assets	0.18%	0.11%	0.10%	0.04%	0.04%

Real Estate Owned (REO). The Bank aggressively markets any REO properties, when and if, they are acquired through foreclosure. At December 31, 2007, 2006 and 2005, the Bank did not own any such properties.

Environmental Concerns Relating to Loans. The Bank currently obtains environmental reports in connection with the underwriting of commercial real estate loans, and typically obtains environmental reports in connection with the underwriting of multi-family loans. For all other loans, the Bank obtains environmental reports only if the nature of the current or, to the extent known to the Bank, prior use of the property securing the loan indicates a potential environmental risk. However, the Bank may not be aware of such uses or risks in any particular case, and, accordingly, there is no assurance that real estate acquired by the Bank in foreclosure is free from environmental contamination or that, if any such contamination or other violation exists, the Bank will not have any liability therefor.

Allowance for Loan Losses

The Bank has established and maintains on its books an allowance for loan losses that is designed to provide a reserve against estimated losses inherent in the Bank s overall loan portfolio. The allowance is established through a provision for loan losses based on management s evaluation of the risk inherent in the various components of its loan portfolio and other factors, including historical loan loss experience (which is updated at least annually), changes in the composition and volume of the portfolio, collection policies and experience, trends in the volume of non-accrual loans and regional and national economic conditions. The determination of the amount of the allowance for loan losses includes estimates that are susceptible to significant changes due to changes in appraisal values of collateral, national and regional economic conditions and other factors. Management reviews the Bank s loan portfolio by separate categories with similar risk and collateral characteristics. Impaired loans are segregated and reviewed separately. All non-performing loans are classified impaired. Impaired loans secured by collateral are reviewed based on their collateral and the estimated time to recover the Bank s investment in the loan, and the estimate of the recovery

anticipated. Specific reserves allocated to impaired loans were $605,000 and $316,000 at December 31, 2007 and 2006, respectively. For non-collateralized impaired loans, management estimates any recoveries that are anticipated for each loan. Specific reserves are allocated to impaired loans based on this review. In connection with the determination of the allowance, the market value of collateral ordinarily is evaluated by the Bank s staff appraiser; however, the Bank may from time to time obtain independent appraisals for significant properties. Current year charge-offs, charge-off trends, new loan production and current balance by particular loan categories are also taken into account in determining the appropriate amount of

allowance. The Board of Directors reviews and approves the adequacy of the allowance for loan losses on a quarterly basis.

In assessing the adequacy of the allowance, management also reviews the Bank s loan portfolio by separate categories which have similar risk and collateral characteristics; e.g. multi-family residential, commercial real estate, one-to-four family mixed-use property, one-to-four family residential, co-operative apartment, construction, SBA, commercial business, taxi medallion and consumer loans. General provisions are established against performing loans in the Bank s portfolio in amounts deemed prudent from time to time based on the Bank s qualitative analysis of the factors, including the historical loss experience and regional economic conditions. During the five-year period ended December 31, 2007, the Bank incurred total net charge-offs of $701,000. This reflects a significant improvement over the loss experience of the 1990s. In addition, while the regional economy had slowed by the fourth quarter of 2007, the regional economy has improved since 2001, including significant increases in real estate values. The Bank s underwriting standards generally require a loan-to-value ratio of 75% at a time the loan is originated. Since real estate values have increased significantly since 2001, the loan-to-value ratios for loans originated in prior years have declined below the original 75% level. The rate at which mortgagors have been defaulting on their loans has declined, as the mortgagor s equity in the property has increased. The Bank has not been affected by the recent increase in defaults of sub-prime mortgages as the Bank does not originate, or hold in portfolio, sub-prime mortgages. As a result, the Bank has not incurred losses on mortgage loans in recent years. As a result of these improvements, and despite the increase in the loan portfolio and shift to loans with greater risk, the Bank has not considered it necessary to provide a provision for loan losses during any of the years in the five-year period ended December 31, 2007. Management has concluded, and the Board of Directors has concurred, that, during this time period, the allowance was sufficient to absorb losses inherent in the loan portfolio.

The Bank s determination as to the classification of its assets and the amount of its valuation allowances is subject to review by the OTS and the FDIC, which can require the establishment of additional general allowances or specific loss allowances or require charge-offs. Such authorities may require the Bank to make additional provisions to the allowance based on their judgments about information available to them at the time of their examination. An OTS policy statement provides guidance for OTS examiners in determining whether the levels of general valuation allowances for savings institutions are adequate. The policy statement requires that if a savings institution s general valuation allowance policies and procedures are deemed to be inadequate, recommendations for correcting deficiencies, including any examiner concerns regarding the level of the allowance, should be noted in the report of examination. Additional supervisory action may also be taken based on the magnitude of the observed shortcomings in the allowance process, including the materially of any error in the reported amount of the allowance.

Management of the Bank believes that the current allowance for loan losses is adequate in light of current economic conditions, the composition of its loan portfolio and other available information and the Board of Directors concurs in this belief. Due to the acquisition of Atlantic Liberty in 2006, the allowance for loan losses was increased by Atlantic Liberty s allowance of $753,000. The Bank however did not record any additional provision for loan losses for the years ended December 31, 2007, 2006 and 2005. At December 31, 2007, the total allowance for loan losses was $6.6 million, representing 112.57% of each of non-performing loans and non-performing assets, compared to 225.72% for both of these ratios at December 31, 2006. The Bank continues to monitor and, as necessary, modify the level of its allowance for loan losses in order to maintain the allowance at a level which management considers adequate to provide for probable loan losses based on available information.

Many factors may require additions to the allowance for loan losses in future periods beyond those currently revealed. These factors include future adverse changes in economic conditions, changes in interest rates and changes in the financial capacity of individual borrowers (any of which may affect the ability of borrowers to make repayments on loans), changes in the real estate market within the Bank s lending area and the value of collateral, or a review and evaluation of the Bank s loan portfolio in the future. The determination of the amount of the allowance for loan losses includes estimates that are susceptible to significant changes due to changes in appraised values of collateral, national and regional economic conditions, interest rates and other factors. In addition, the Bank s increased emphasis on multi-family residential, commercial real estate and one-to-four family mixed-use property mortgage loans can be expected to increase the overall level of credit risk inherent in the Bank s loan portfolio. The greater risk associated with these loans, as well as construction loans and business loans, could require the Bank to increase its provisions for loan losses and to maintain an allowance for loan losses as a percentage of total loans that is in excess of the allowance currently maintained by the Bank. Provisions for loan losses are charged against net income. See Lending Activities and Asset Quality.

The following table sets forth changes in, and the balance of, the Bank s allowance for loan losses.

	At and for the years ended December 31,				
(Dollars in thousands)	2007	2006	2005	2004	2003
Balance at beginning of year	$ 7,057	$ 6,385	$ 6,533	$ 6,553	$ 6,581
Acquisition of Atlantic Liberty		753			
Provision for loan losses					
Loans charged-off:					
Multi-family residential					
Commercial real estate					
One-to-four family mixed-use property					
One-to-four family residential					
Co-operative apartment					
Construction					
SBA	(470)	(57)	(144)	(28)	(111)
Commercial business and other loans	(2)	(36)	(20)		(44)
Total loans charged-off	(472)	(93)	(164)	(28)	(155)
Recoveries:					
Mortgage loans	29	2	3	3	125
SBA, commercial business and other loans	19	10	13	5	2
Total recoveries	48	12	16	8	127
Net charge-offs	(424)	(81)	(148)	(20)	(28)
Balance at end of year	$ 6,633	$ 7,057	$ 6,385	$ 6,533	$ 6,553
Ratio of net charge-offs during the year to average loans outstanding during the year	0.02%	0.00%	0.01%	0.00%	0.00%
Ratio of allowance for loan losses to gross loans at end of the year	0.25%	0.30%	0.34%	0.43%	0.51%
Ratio of allowance for loan losses to non-performing loans at the end of the year	112.57%	225.72%	260.39%	717.29%	960.86%
Ratio of allowance for loan losses to non-performing assets at the end of the year	112.57%	225.72%	260.39%	717.29%	960.86%

The following table sets forth the Bank s allocation of its allowance for loan losses to the total amount of loans in each of the categories listed at the dates indicated. The numbers contained in the Amount column indicate the allowance for loan losses allocated for each particular loan category. The numbers contained in the column entitled Percentage of Loans in Category to Total Loans indicate the total amount of loans in each particular category as a percentage of the Bank s loan portfolio.

	At December 31,									
	2007		2006		2005		2004		2003	
Loan Category	Amount	Percent of Loans in Category to Total loans	Amount	Percent of Loans in Category to Total loans	Amount	Percent of Loans in Category to Total loans	Amount	Percent of Loans in Category to Total loans	Amount	Percent of Loans in Category to Total loans
	(Dollars in thousands)									
Mortgage Loans:										
Multi-family residential	$ 1,644	35.79%	$ 1,122	37.52%	$ 1,216	41.92%	$ 1,010	42.61%	$ 1,251	42.53%
Commercial real estate	933	23.23	668	22.38	1,272	21.23	1,715	22.00	2,740	22.79
One-to-four family mixed-use property	1,223	25.49	661	25.33	1,544	25.42	1,494	21.92	803	17.76
One-to-four family residential	251	6.01	80	6.98	524	7.17	718	10.00	684	14.01
Co-operative apartment	15	0.26	10	0.35	161	0.11	207	0.21	127	0.29
Construction	1,172	4.44	851	4.50	64	2.63	55	2.07	56	1.85
Gross mortgage loans	5,238	95.22	3,392	97.06	4,781	98.48	5,199	98.81	5,661	99.23
Small Business Administration loans	373	0.70	1,895	0.75	964	0.49	663	0.37	553	0.39
Commercial business and other loans	1,022	4.08	1,770	2.19	640	1.03	671	0.82	339	0.38
Total loans	$ 6,633	100.00%	$ 7,057	100.00%	$ 6,385	100.00%	$ 6,533	100.00%	$ 6,553	100.00%

Investment Activities

General. The investment policy of the Company, which is approved by the Board of Directors, is designed primarily to manage the interest rate sensitivity of its overall assets and liabilities, to generate a favorable return without incurring undue interest rate and credit risk, to complement the Bank s lending activities and to provide and maintain liquidity. In establishing its investment strategies, the Company considers its business and growth strategies, the economic environment, its interest rate risk exposure, its interest rate sensitivity gap position, the types of securities to be held, and other factors. See Management s Discussion and Analysis of Financial Condition and Results of Operations Overview Management Strategy in Item 7 of this Annual Report.

Federally chartered savings institutions have authority to invest in various types of assets, including U.S. government obligations, securities of various federal agencies, mortgage-backed and mortgage-related securities, certain certificates of deposit of insured banks and savings institutions, certain bankers acceptances, reverse repurchase agreements, loans of federal funds, and, subject to certain limits, corporate securities, commercial paper and mutual funds. The Company primarily invests in mortgage-backed securities, U. S. government obligations, and mutual funds which purchase these same instruments.

The Investment Committee of the Bank and the Company meets quarterly to monitor investment transactions and to establish investment strategy. The Board of Directors reviews the investment policy on an annual basis and investment activity on a monthly basis.

The Company classifies its investment securities as available for sale. Unrealized gains and losses (other than unrealized losses considered other than temporary) for available-for-sale securities are excluded from earnings and included in Accumulated Other Comprehensive Income (a separate component of equity), net of taxes. At December 31, 2007, the Company had $440.1 million in securities available for sale which represented 13.1% of total assets. These securities had an aggregate market value at December 31, 2007 that was approximately 1.9 times the amount of the Company s equity at that date. The cumulative balance of unrealized net gains on securities available for sale was $16,000, net of taxes, at December 31, 2007. As a result of the magnitude of the Company s holdings of securities available for sale, changes in interest rates could produce significant changes in the value of such securities and could produce significant fluctuations in the equity of the Company. See Note 4 of Notes to Consolidated Financial Statements, included in Item 8 of this Annual Report. The Company may from time to time sell securities and realize a loss if the proceeds of such sale may be reinvested in loans or other assets offering more attractive yields.

At December 31, 2007, there was one issuer s security, excluding government agencies or government sponsored agencies, that either alone, or together with any investments in the securities of any affiliate(s) of such issuer, exceeded 10% of the Company s equity. This security is a collateralized mortgage obligation issued by Residential Asset Securitization Trust 2006-A4IP, and is a senior fixed-rate pass-through whose credit enhancement is the securities subordinated to this security. The Company s amortized cost of this security as of December 31, 2007 was $24.7 million, and the fair value of the security was $24.4 million. The Company does not consider this investment to be other-than-temporarily impaired as of December 31, 2007.

The table below sets forth certain information regarding the amortized cost and market values of the Company s securities portfolio, interest bearing deposits and federal funds sold, at the dates indicated. Securities available for sale are recorded at market value. See Note 4 of Notes to Consolidated Financial Statements, included in Item 8 of this Annual Report.

	At December 31,					
	2007		2006		2005	
	Amortized Cost	Market Value	Amortized Cost	Market Value	Amortized Cost	Market Value
	(In thousands)					
Securities available for sale						
Bonds and other debt securities:						
U.S. government and agencies	$ 4,406	$ 4,406	$ 15,016	$ 15,004	$ 10,942	$ 10,911
Corporate debentures	2,643	2,643				
Total bonds and other debt securities	7,049	7,049	15,016	15,004	10,942	10,911
Mutual funds	21,752	21,752	21,224	20,645	20,296	19,767
Equity securities:						
Common stock	1,838	1,838	619	619	619	619
Preferred stock	46,732	46,732	5,685	5,468	5,493	5,270
Total equity securities	48,570	48,570	6,304	6,087	6,112	5,889
Mortgage-backed securities:						
FNMA	123,121	122,770	135,458	131,192	152,412	147,802
REMIC and CMO	182,609	182,730	100,165	98,652	91,369	89,561
FHLMC	45,511	45,566	53,440	51,733	57,470	55,735
GNMA	11,464	11,663	7,199	7,274	7,789	8,096
Total mortgage-backed securities	362,705	362,729	296,262	288,851	309,040	301,194
Total securities available for sale	440,076	440,100	338,806	330,587	346,390	337,761
Interest-bearing deposits and Federal funds sold	5,758	5,758	4,670	4,670	4,396	4,396
Total	$ 445,834	$ 445,858	$ 343,476	$ 335,257	$ 350,786	$ 342,157

Mortgage-backed securities. At December 31, 2007, the Company had $362.7 million invested in mortgage-backed securities, of which $13.5 million was invested in adjustable-rate mortgage-backed securities. The mortgage loans underlying these adjustable-rate securities generally are subject to limitations on annual and lifetime interest rate increases. The Company anticipates that investments in mortgage-backed securities may continue to be used in the future to supplement mortgage-lending activities. Mortgage-backed securities are more liquid than individual mortgage loans and may be used more easily to collateralize obligations of the Bank.

The following table sets forth the Company s mortgage-backed securities purchases, sales and principal repayments for the years indicated:

	For the years ended December 31,		
	2007	2006	2005
		(In thousands)	
Balance at beginning of year	$ 288,851	$ 301,194	$ 395,629
Acquired with Atlantic Liberty		30,844	
Purchases of mortgage-backed securities	117,408	43,897	29,627
Amortization of unearned premium, net of accretion of unearned discount	(193)	(560)	(1,219)
Net change in unrealized gains (losses) on mortgage-backed securities available for sale	1,695	435	(6,285)
Net realized gains recorded on mortgage-backed securities carried at fair value	2,685		
Net change in interest due on securities carried at fair value	515		
Sales of mortgage-backed securities		(36,220)	(28,643)
Principal repayments received on mortgage-backed securities	(48,232)	(50,739)	(87,915)
Net increase (decrease) in mortgage-backed securities	73,878	(12,343)	(94,435)
Balance at end of year	$ 362,729	$ 288,851	$ 301,194

While mortgage-backed securities carry a reduced credit risk as compared to whole loans, such securities remain subject to the risk that a fluctuating interest rate environment, along with other factors such as the geographic distribution of the underlying mortgage loans, may alter the prepayment rate of such mortgage loans and so affect both the prepayment speed and value of such securities. The Company does not own any derivative instruments that are extremely sensitive to changes in interest rates.

The table below sets forth certain information regarding the amortized cost, fair value, annualized weighted average yields and maturities of the Company s debt and equity securities at December 31, 2007. The stratification of balances is based on stated maturities. Equity securities are shown as immediately maturing, except for preferred stocks with stated redemption dates, which are shown in the period they are scheduled to be redeemed. Assumptions for repayments and prepayments are not reflected for mortgage-backed securities. The Company carries these investments at their fair value in the consolidated financial statements.

	One year or Less		One to Five Years		Five to Ten Years		More than Ten Years		Total Securities			
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Average Remaining Years to Maturity	Amortized Cost	Estimated Fair Value	Weighted Average Yield
	(Dollars in thousands)											
Securities available for sale												
Bonds and other debt securities:												
U.S. government and agencies	$	%	$	%	$ 4,406	4.15%	$	%	5.16	$ 4,406	$ 4,406	4.15%
Corporate debentures					2,643	5.39			4.63	2,643	2,643	5.39
Total bonds and other debt securities					7,049	4.61			4.96	7,049	7,049	4.61
Mutual funds	21,752	4.99							N/A	21,752	21,752	4.99
Equity securities:												
Common stock							1,838	7.03	N/A	1,838	1,838	7.03
Preferred stock					4,753	5.78	41,979	7.18	N/A	46,732	46,732	7.04
Total equity securities					4,753	5.78	43,817	7.17	N/A	48,570	48,570	7.04
Mortgage-backed securities:												
FNMA			4,114	5.01	8,318	5.33	110,689	5.08	16.38	123,121	122,770	5.09

REMIC and CMO	$(11,979)	$27	$ 71,712

NOTE 9—CONTINGENCIES

In the ordinary course of business, the Company is a party to various lawsuits. The Company establishes reserves for specific legal matters when it determines that the likelihood of an unfavorable outcome is probable and the loss is reasonably estimable. Management has also identified certain other legal matters where we believe an unfavorable outcome is not probable and, therefore, no reserve is established. Although management currently believes that resolving claims against us, including claims where an unfavorable outcome is reasonably possible, will not have a material impact on the liquidity, results of operations, or financial condition of the Company, these matters are subject to inherent uncertainties and management's view of these matters may change in the future. The Company also evaluates other contingent matters, including income and non-income tax contingencies, to assess the likelihood of an unfavorable outcome and estimated extent of potential loss. It is possible that an unfavorable outcome of one or more of these lawsuits or other contingencies could have a material impact on the liquidity, results of operations, or financial condition of the Company. See Note 2 for additional information related to income tax contingencies.

NOTE 10—GUARANTOR AND NON-GUARANTOR FINANCIAL INFORMATION

The 2013 and 2012 Senior Notes are unconditionally guaranteed, jointly and severally, by certain domestic subsidiaries which are 100% owned by the Company. The following tables present condensed consolidating financial information at March 31, 2015 and December 31, 2014 and for the three months ended March 31, 2015 and 2014 for: IAC, on a stand-alone basis; the combined guarantor subsidiaries of IAC; the combined non-guarantor subsidiaries of IAC; and IAC on a consolidated basis.

IAC/INTERACTIVECORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Balance sheet at March 31, 2015:

	IAC	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Total Eliminations	IAC Consolidated
	(In thousands)				
Cash and cash equivalents	$468,857	$—	$ 202,740	$—	$671,597
Marketable securities	204,700	—	921	—	205,621
Accounts receivable, net	17	156,409	76,038	—	232,464
Other current assets	41,743	93,861	54,186	(5,529)	184,261
Intercompany receivables	—	1,732,085	982,713	(2,714,798)	—
Property and equipment, net	5,511	229,513	62,932	—	297,956
Goodwill	—	1,250,200	470,701	—	1,720,901
Intangible assets, net	—	319,502	150,050	—	469,552
Investment in subsidiaries	5,056,128	916,116	—	(5,972,244)	—
Other non-current assets	44,460	21,042	112,382	(2,131)	175,753
Total assets	$5,821,416	$4,718,728	$ 2,112,663	$(8,694,702)	$3,958,105
Accounts payable, trade	$3,954	$56,934	$ 22,558	$—	$83,446
Other current liabilities	44,152	318,375	180,402	(623)	542,306
Long-term debt	1,000,000	80,000	—	—	1,080,000
Income taxes payable	909	4,777	23,614	—	29,300
Intercompany liabilities	2,714,798	—	—	(2,714,798)	—
Other long-term liabilities	304,889	104,257	39,935	(7,037)	442,044
Redeemable noncontrolling interests	—	—	28,295	—	28,295
IAC shareholders' equity	1,752,714	4,154,385	1,817,859	(5,972,244)	1,752,714
Total liabilities and shareholders' equity	$5,821,416	$4,718,728	$ 2,112,663	$(8,694,702)	$3,958,105

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IAC/INTERACTIVECORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Balance sheet at December 31, 2014:

	IAC	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Total Eliminations	IAC Consolidated
	(In thousands)				
Cash and cash equivalents	$766,076	$1,021	$223,308	$—	$990,405
Marketable securities	159,197	—	1,451	—	160,648
Accounts receivable, net	13	155,262	80,811	—	236,086
Other current assets	23,923	91,105	57,487	(5,773)	166,742
Intercompany receivables	—	1,688,403	970,810	(2,659,213)	—
Property and equipment, net	4,950	232,819	64,690	—	302,459
Goodwill	—	1,249,807	505,119	—	1,754,926
Intangible assets, net	—	325,771	166,165	—	491,936
Investment in subsidiaries	5,035,304	930,443	—	(5,965,747)	—
Other non-current assets	44,610	20,682	109,372	(2,988)	171,676
Total assets	$6,034,073	$4,695,313	$2,179,213	$(8,633,721)	$4,274,878
Accounts payable, trade	$3,059	$55,320	$22,784	$—	$81,163
Other current liabilities	73,491	328,920	191,197	(817)	592,791
Long-term debt	1,000,000	80,000	—	—	1,080,000
Income taxes payable	2,240	4,771	25,624	—	32,635
Intercompany liabilities	2,659,213	—	—	(2,659,213)	—
Other long-term liabilities	304,117	104,219	54,328	(7,944)	454,720
Redeemable noncontrolling interests	—	—	40,427	—	40,427
IAC shareholders' equity	1,991,953	4,122,083	1,843,664	(5,965,747)	1,991,953
Noncontrolling interests	—	—	1,189	—	1,189
Total liabilities and shareholders' equity	$6,034,073	$4,695,313	$2,179,213	$(8,633,721)	$4,274,878

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IAC/INTERACTIVECORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Statement of operations for the three months ended March 31, 2015:

	IAC	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Total Eliminations	IAC Consolidated
	(In thousands)				
Revenue	$—	$594,801	$180,360	$(2,649)	$772,512
Operating costs and expenses:					
Cost of revenue (exclusive of depreciation shown separately below)	245	119,741	71,764	(197)	191,553
Selling and marketing expense	1,055	288,625	70,396	(2,410)	357,666
General and administrative expense	24,064	65,753	25,019	(42)	114,794
Product development expense	2,177	31,134	11,946	—	45,257
Depreciation	401	11,580	3,587	—	15,568
Amortization of intangibles	—	6,270	6,285	—	12,555
Total operating costs and expenses	27,942	523,103	188,997	(2,649)	737,393
Operating (loss) income	(27,942)	71,698	(8,637)	—	35,119
Equity in earnings of unconsolidated affiliates	54,124	3,696	—	(57,820)	—
Interest expense	(12,990)	(1,046)	(28)	—	(14,064)
Other (expense) income, net	(9,353)	11,392	4,949	—	6,988
Earnings (loss) from continuing operations before income taxes	3,839	85,740	(3,716)	(57,820)	28,043
Income tax benefit (provision)	22,441	(31,796)	3,175	—	(6,180)
Earnings (loss) from continuing operations	26,280	53,944	(541)	(57,820)	21,863
Earnings from discontinued operations, net of tax	125	—	—	—	125
Net earnings (loss)	26,405	53,944	(541)	(57,820)	21,988
Net loss attributable to noncontrolling interests	—	—	4,417	—	4,417
Net earnings attributable to IAC shareholders	$26,405	$53,944	$3,876	$(57,820)	$26,405
Comprehensive (loss) income attributable to IAC shareholders	$(29,168)	$48,159	$(52,868)	$4,709	$(29,168)

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IAC/INTERACTIVECORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Statement of operations for the three months ended March 31, 2014:

	IAC	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Total Eliminations	IAC Consolidated
	(In thousands)				
Revenue	$—	$546,326	$196,907	$(2,986)	$740,247
Operating costs and expenses:					
Cost of revenue (exclusive of depreciation shown separately below)	(28)	129,301	80,921	(960)	209,234
Selling and marketing expense	192	236,341	63,764	(1,698)	298,599
General and administrative expense	22,446	45,675	26,955	13	95,089
Product development expense	1,471	27,096	10,590	(341)	38,816
Depreciation	329	9,561	4,928	—	14,818
Amortization of intangibles	—	9,001	2,978	—	11,979
Total operating costs and expenses	24,410	456,975	190,136	(2,986)	668,535
Operating (loss) income	(24,410)	89,351	6,771	—	71,712
Equity in earnings of unconsolidated affiliates	54,297	932	—	(55,229)	—
Interest expense	(12,985)	(1,042)	(37)	—	(14,064)
Other income (expense), net	9,685	(10,527)	(1,116)	—	(1,958)
Earnings from continuing operations before income taxes	26,587	78,714	5,618	(55,229)	55,690
Income tax benefit (provision)	10,112	(29,944)	(1,553)	—	(21,385)
Earnings from continuing operations	36,699	48,770	4,065	(55,229)	34,305
Loss from discontinued operations, net of tax	(814)	—	(13)	13	(814)
Net earnings	35,885	48,770	4,052	(55,216)	33,491
Net loss attributable to noncontrolling interests	—	—	2,394	—	2,394
Net earnings attributable to IAC shareholders	$35,885	$48,770	$6,446	$(55,216)	$35,885
Comprehensive income attributable to IAC shareholders	$41,234	$49,153	$10,115	$(59,268)	$41,234

IAC/INTERACTIVECORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Statement of cash flows for the three months ended March 31, 2015:

	IAC	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	IAC Consolidated
	(In thousands)			
Net cash (used in) provided by operating activities attributable to continuing operations	$(53,803)	$87,776	$(37,783)	$(3,810)
Cash flows from investing activities attributable to continuing operations:				
Acquisitions, net of cash acquired	—	(3,002)	(2,707)	(5,709)
Capital expenditures	(935)	(8,530)	(3,411)	(12,876)
Proceeds from maturities and sales of marketable debt securities	6,050	—	—	6,050
Purchases of marketable debt securities	(47,930)	—	—	(47,930)
Purchases of long-term investments	—	—	(8,345)	(8,345)
Other, net	3,615	(356)	(416)	2,843
Net cash used in investing activities attributable to continuing operations	(39,200)	(11,888)	(14,879)	(65,967)
Cash flows from financing activities attributable to continuing operations:				
Purchase of treasury stock	(200,000)	—	—	(200,000)
Dividends	(28,675)	—	—	(28,675)
Issuance of common stock, net of withholding taxes	(10,339)	—	—	(10,339)
Excess tax benefits from stock-based awards	16,715	—	131	16,846
Purchase of noncontrolling interests	—	—	(15,338)	(15,338)
Acquisition-related contingent consideration payment	—	(180)	—	(180)
Intercompany	18,083	(76,739)	58,656	—
Other, net	—	—	110	110
Net cash (used in) provided by financing activities attributable to continuing operations	(204,216)	(76,919)	43,559	(237,576)
Total cash used in continuing operations	(297,219)	(1,031)	(9,103)	(307,353)
Effect of exchange rate changes on cash and cash equivalents	—	10	(11,465)	(11,455)
Net decrease in cash and cash equivalents	(297,219)	(1,021)	(20,568)	(318,808)
Cash and cash equivalents at beginning of period	766,076	1,021	223,308	990,405
Cash and cash equivalents at end of period	$468,857	$—	$202,740	$671,597

IAC/INTERACTIVECORP
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

Statement of cash flows for the three months ended March 31, 2014:

	IAC	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	IAC Consolidated
	(In thousands)			
Net cash (used in) provided by operating activities attributable to continuing operations	$(29,300)	$72,253	$(312)	$42,641
Cash flows from investing activities attributable to continuing operations:				
Acquisitions, net of cash acquired	—	(54,483)	(23,498)	(77,981)
Capital expenditures	(985)	(5,931)	(2,805)	(9,721)
Purchases of marketable debt securities	(32,848)	—	—	(32,848)
Purchases of long-term investments	(3,000)	(3,286)	(1,575)	(7,861)
Other, net	2	—	(159)	(157)
Net cash used in investing activities attributable to continuing operations	(36,831)	(63,700)	(28,037)	(128,568)
Cash flows from financing activities attributable to continuing operations:				
Dividends	(20,004)	—	—	(20,004)
Issuance of common stock, net of withholding taxes	920	—	—	920
Excess tax benefits from stock-based awards	15,610	—	8,593	24,203
Purchase of noncontrolling interests	—	(30,000)	—	(30,000)
Funds returned from escrow for Meetic tender offer	—	—	12,354	12,354
Intercompany	(41,436)	21,448	19,988	—
Other, net	(374)	—	79	(295)
Net cash (used in) provided by financing activities attributable to continuing operations	(45,284)	(8,552)	41,014	(12,822)
Total cash (used in) provided by continuing operations	(111,415)	1	12,665	(98,749)
Effect of exchange rate changes on cash and cash equivalents	—	(1)	1,617	1,616
Net (decrease) increase in cash and cash equivalents	(111,415)	—	14,282	(97,133)
Cash and cash equivalents at beginning of period	782,022	—	318,422	1,100,444
Cash and cash equivalents at end of period	$670,607	$—	$332,704	$1,003,311

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

GENERAL

Management Overview

IAC is a leading media and Internet company. The Company is organized into four segments: The Match Group, which consists of dating, education and fitness businesses with brands such as Match, OkCupid, Tinder, The Princeton Review and DailyBurn; Search & Applications, which includes brands such as About.com, Ask.com, Dictionary.com and Investopedia; Media, which includes businesses such as Vimeo, Electus, The Daily Beast and CollegeHumor; and eCommerce, which includes HomeAdvisor and ShoeBuy. IAC's brands and products are among the most recognized in the world, reaching users in over 200 countries.

For a more detailed description of the Company's operating businesses, see the Company's annual report on Form 10-K for the year ended December 31, 2014.

A substantial portion of the Company's revenue is derived from online advertising. Most of the Company's online advertising revenue is attributable to our services agreement with Google Inc. ("Google"), which expires on March 31, 2016. Our services agreement requires that we comply with certain guidelines promulgated by Google. Subject to certain limitations, Google may unilaterally update its policies and guidelines, which could require modifications to, or prohibit and/or render obsolete certain of our products, services and/or business practices, which could be costly to address or otherwise have an adverse effect on our business, financial condition and results of operations. For the three months ended March 31, 2015 and 2014, revenue earned from Google is $339.6 million and $355.6 million, respectively. This revenue is earned by the businesses comprising the Search & Applications segment.

Factors Affecting Results

For the three months ended March 31, 2015, the Company delivered 4% revenue growth; however, Adjusted EBITDA and operating income declined 30% and 51%, respectively. The revenue increase was driven by solid growth from The Match Group, Media and eCommerce, partially offset by a modest decrease at Search & Applications; while declines in Adjusted EBITDA and operating income were driven by increased investment at The Match Group, Media and eCommerce and lower revenue at Search & Applications, partially offset by lower Corporate expenses.

Revenue from The Match Group segment benefited from the contributions of The Princeton Review, which was acquired on August 1, 2014, and FriendScout24, which was acquired on August 31, 2014, and increased Dating paid subscribers, partially offset by foreign exchange effects. Within Media and eCommerce, additional investments in marketing and headcount at Vimeo and HomeAdvisor, respectively, increased its revenue and losses. The revenue from Search & Applications decreased due primarily to a decline at Websites.

The Match Group Adjusted EBITDA decreased due to increased investment in marketing, losses from The Princeton Review and $3.3 million of costs in the current year related to our ongoing consolidation and streamlining of technology systems and European operations at our Dating businesses. Adjusted EBITDA from Search & Applications decreased due to lower revenue and the impact of the write-off of $2.3 million of deferred revenue in connection with the acquisition of SlimWare, which was acquired on April 1, 2014.

Results of Operations for the three months ended March 31, 2015 compared to the three months ended March 31, 2014

Revenue

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Search & Applications	$382,898	$(15,137)	(4)%	$398,035
The Match Group	239,211	28,024	13%	211,187
Media	43,612	7,257	20%	36,355
eCommerce	107,010	12,168	13%	94,842
Inter-segment elimination	(219)	(47)	(27)%	(172)
Total	$772,512	$32,265	4%	$740,247

Search & Applications revenue decreased 4% reflecting declines from Websites (which is principally composed of Ask.com, About.com, CityGrid, Dictionary.com, Investopedia, PriceRunner and Ask.fm) and Applications (which includes our direct-to-consumer downloadable desktop search and mobile applications operations ("B2C") and our partnership operations ("B2B")). Websites revenue decreased 7% to $189.7 million due primarily to a decline in revenue at Ask.com, partially offset by strong growth at About.com. Applications revenue decreased 1% to $193.2 million due to lower queries from our B2B operations, partially offset by strength from our B2C operations, including query growth in our desktop search applications, as well as the contribution from mobile applications (via our acquisition of Apalon on November 3, 2014) and SlimWare.

The Match Group revenue increased 13%, or 19% excluding the effects of foreign exchange, driven by a 2% increase in Dating revenue and 372% increase in non-dating revenue. Dating North America (which includes Match, Chemistry, People Media, OkCupid, Tinder and other dating businesses operating within the United States and Canada) revenue increased 8% to $145.2 million driven by a 13% increase in paid subscribers. This increase in Dating North America revenue was partially offset by an 8% decrease in Dating International (which includes Meetic, Tinder's international operations and all other dating businesses operating outside of the United States and Canada) revenue, despite a 21% increase in paid subscribers, due to foreign exchange effects. Excluding foreign exchange effects, total Dating revenue and Dating International revenue would have increased 8% and 9%, respectively. Non-dating (consisting of The Princeton Review, Tutor.com and DailyBurn) revenue benefited from the acquisition of The Princeton Review.

Media revenue increased 20% due principally to the contribution from IAC Films and solid growth at Vimeo. IAC Films released the movie While We're Young in theaters in March 2015.

eCommerce revenue increased 13% due to 24% growth at HomeAdvisor driven by domestic revenue and service requests increasing 34% and 38%, respectively.

Cost of revenue

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Cost of revenue (exclusive of depreciation shown separately below)	$191,553	$(17,681)	(8)%	$209,234
As a percentage of revenue	25%			28%

Cost of revenue consists primarily of traffic acquisition costs and includes payments made to partners who distribute our B2B customized browser-based applications, integrate our paid listings into their websites or direct traffic to our websites. These payments include amounts based on revenue share and other arrangements. Cost of revenue also includes ShoeBuy's cost of products sold and shipping and handling costs, production costs related to media produced by Electus and other businesses within our Media segment, content acquisition costs, expenses associated with the operation of the Company's data centers, including compensation (including stock-based compensation) and other employee-related costs for personnel engaged in data center functions, rent, energy and hosting fees.

Cost of revenue in 2015 decreased from 2014 due to a decrease of $37.1 million from Search & Applications, partially offset by increases of $13.1 million from The Match Group and $7.1 million from Media.

- The Search & Applications decrease was primarily due to a reduction of $38.2 million in traffic acquisition costs driven by a decline in revenue at Ask.com and our B2B operations.
- The Match Group increase was primarily due to the acquisition of The Princeton Review and increases in revenue share payments made in connection with in-app purchases sold through Dating's mobile products and hosting fees.
- The Media increase was primarily due to production costs at IAC Films related to the release of the movie While We're Young in March 2015.

Selling and marketing expense

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Selling and marketing expense	$357,666	$59,067	20%	$298,599
As a percentage of revenue	46%			40%

Selling and marketing expense consists primarily of advertising expenditures and compensation (including stock-based compensation) and other employee-related costs for personnel engaged in sales, sales support and customer service functions. Advertising expenditures include online marketing, including fees paid to search engines and third parties that distribute our B2C downloadable applications, and offline marketing, which is primarily television advertising.

Selling and marketing expense in 2015 increased from 2014 due to increases of $21.9 million from Search & Applications, $15.7 million from eCommerce, $15.3 million from The Match Group and $5.4 million from Media.

- The Search & Applications increase was primarily due to a $22.6 million increase in online marketing, which was primarily related to the growth in About.com and the acquisition of SlimWare, partially offset by a decline at Ask.com.
- The eCommerce increase was primarily due to increases of $9.9 million in offline and online marketing principally related to HomeAdvisor and $5.3 million in compensation due, in part, to increased headcount at HomeAdvisor.
- The Match Group increase was primarily due to an increase of $11.9 million in online and offline marketing at Dating and DailyBurn and the acquisition of The Princeton Review.
- The Media increase was primarily due to an increase of $4.4 million in online marketing at Vimeo.

General and administrative expense

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
General and administrative expense	$114,794	$19,705	21%	$95,089
As a percentage of revenue	15%			13%

General and administrative expense consists primarily of compensation (including stock-based compensation) and other employee-related costs for personnel engaged in executive management, finance, legal, tax and human resources, facilities costs and fees for professional services.

General and administrative expense in 2015 increased from 2014 due to increases of $7.1 million from The Match Group, $6.9 million from Search & Applications, $2.9 million from eCommerce and $2.0 million from Corporate.

- The Match Group increase was primarily due to the acquisition of The Princeton Review, a $3.9 million benefit in the prior year related to the expiration of the statute of limitations for a non-income tax matter, an increase in compensation and costs in the current year related to our ongoing consolidation and streamlining of technology

systems and European operations at our Dating businesses, partially offset by a decrease of $11.0 million in acquisition-related contingent consideration fair value adjustments. The increase in compensation was primarily due to an increase in headcount due, in part, to the acquisition of FriendScout24.

- The Search & Applications increase was primarily due to acquisitions and $4.0 million in acquisition-related contingent consideration fair value adjustments.
- The eCommerce increase was primarily due to increases in compensation and employee-related costs as a result of increased headcount, and an increase in bad debt expense at HomeAdvisor.
- The Corporate increase was primarily due to an increase in compensation expense, as a result of an increase in stock-based compensation, which was driven by a higher number of forfeited awards in the prior year and the impact of a modification of certain awards in the current year.

Product development expense

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Product development expense	$45,257	$6,441	17%	$38,816
As a percentage of revenue	6%			5%

Product development expense consists primarily of compensation (including stock-based compensation) and other employee-related costs that are not capitalized for personnel engaged in the design, development, testing and enhancement of product offerings and related technology.

Product development expense in 2015 increased from 2014 due to increases of $3.7 million from The Match Group, $0.9 million from eCommerce and $0.8 million from Media.

- The Match Group increase is primarily related to an increase in compensation.
- The eCommerce increase is primarily related to an increase in compensation at HomeAdvisor due, in part, to increased headcount.
- The Media increase is primarily due to increased headcount at Vimeo.

Depreciation

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Depreciation	$15,568	$750	5%	$14,818
As a percentage of revenue	2%			2%

Depreciation in 2015 increased from 2014 primarily due to acquisitions.

Adjusted EBITDA

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Search & Applications	$78,901	$(3,170)	(4)%	$82,071
The Match Group	25,856	(21,574)	(45)%	47,430
Media	(14,583)	(6,719)	(85)%	(7,864)
eCommerce	(3,137)	(5,941)	NM	2,804
Corporate	(11,880)	4,466	27%	(16,346)
Total	$75,157	$(32,938)	(30)%	$108,095
As a percentage of revenue	10%			15%

NM = not meaningful

Refer to Note 8 to the consolidated financial statements for reconciliations of Adjusted EBITDA to operating income (loss) by reportable segment.

Search & Applications Adjusted EBITDA decreased 4% due primarily to lower revenue, increases in selling and marketing expense and general and administrative expense and losses related to the acquisition of SlimWare, partially offset by a decrease in cost of revenue. The loss from SlimWare was due to the write-off of $2.3 million of deferred revenue in connection with its acquisition on April 1, 2014. The increase in selling and marketing expense was primarily due to an increase in online marketing related to About.com, partially offset by a decline at Ask.com. The increase in general and administrative expense was primarily due to acquisitions. The decrease in cost of revenue was primarily due to a decrease in traffic acquisition costs driven from lower revenue from Ask.com and our B2B operations.

The Match Group Adjusted EBITDA decreased 45% despite higher revenue, primarily due to losses from The Princeton Review, which was not in the prior year period, $3.3 million of costs in the current year related to our ongoing consolidation and streamlining of technology systems and European operations at our Dating businesses and higher selling and marketing expense, cost of revenue, general and administrative expense and product development expense. The increase in selling and marketing expense was primarily due to an increase in online and offline marketing at Dating and DailyBurn. The increase in cost of revenue was primarily due to increases in revenue share payments made in connection with in-app purchases sold through Dating's mobile products and hosting fees. The increase in general and administrative expense was primarily due to an increase in compensation and a $3.9 million benefit in the prior year related to the expiration of the statute of limitations for a non-income tax matter. The increase in product development is primarily due to an increase in compensation.

Media Adjusted EBITDA loss was larger than the prior year, despite higher revenue, primarily due to increased investment in online marketing and increased headcount at Vimeo.

eCommerce Adjusted EBITDA flipped to a loss in the current year, despite higher revenue, principally due to an increased investment in offline and online marketing at HomeAdvisor.

Corporate Adjusted EBITDA loss decreased due to lower compensation.

Operating income (loss)

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Search & Applications	$64,300	$(6,037)	(9)%	$70,337
The Match Group	25,312	(14,491)	(36)%	39,803
Media	(15,352)	(6,786)	(79)%	(8,566)
eCommerce	(6,854)	(5,293)	(339)%	(1,561)
Corporate	(32,287)	(3,986)	(14)%	(28,301)
Total	$35,119	$(36,593)	(51)%	$71,712
As a percentage of revenue	5%			10%

Operating income in 2015 decreased from 2014 due to the decrease of $32.9 million in Adjusted EBITDA described above and increases of $9.3 million in stock-based compensation, $0.8 million in depreciation and $0.6 million in amortization of intangibles, partially offset by a decrease of $7.0 million in acquisition-related contingent consideration fair value adjustments. The increase in stock-based compensation was primarily due to a higher number of forfeited awards in the prior year and the impact of a modification of certain awards in the current year. The decrease in acquisition-related contingent consideration fair value adjustments was the result of an update of the future forecast of earnings and operating metrics related to certain acquired businesses.

At March 31, 2015, there was $189.4 million of unrecognized compensation cost, net of estimated forfeitures, related to all equity-based awards, which is expected to be recognized over a weighted average period of approximately 2.8 years.

Interest expense

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Interest expense	$(14,064)	$—	—%	$(14,064)

Interest expense relates to our 4.875% Senior Notes due November 30, 2018 ("2013 Senior Notes"), 4.75% Senior Notes due December 21, 2012 ("2012 Senior Notes") and 5% New York City Industrial Development Agency Liberty Bonds due September 1, 2035 ("Liberty Bonds").

Other income (expense), net

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Other income (expense), net	$6,988	$8,946	NM	$(1,958)

Other income, net in 2015 primarily includes net foreign currency exchange gains and reduced losses associated with our equity method investments.

Other expense, net in 2014 primarily includes losses associated with our equity method investments.

Income tax provision

	Three Months Ended March 31,			
	2015	$ Change	% Change	2014
	(Dollars in thousands)			
Income tax provision	$(6,180)	NM	NM	$(21,385)
Effective income tax rate	22%			38%

The 2015 effective income tax rate is lower than the statutory rate of 35% due primarily to the non-taxable gain on contingent consideration fair value adjustments in the current year period and a reduction in tax reserves and related interest due to the expiration of statutes of limitations. The 2014 effective income tax rate is higher than the statutory rate of 35% due primarily to interest on reserves for income tax contingencies and state taxes, partially offset by foreign income taxed at lower rates.

The Company recognizes interest and, if applicable, penalties related to unrecognized tax benefits in income tax provision. Included in the income tax provision for continuing operations for the three months ended March 31, 2015 and 2014, is a $0.1 million benefit and a $1.6 million provision, respectively, net of related deferred taxes, for interest on unrecognized tax benefits. At March 31, 2015 and December 31, 2014, the Company has accrued $2.5 million and $2.8 million, respectively, for the payment of interest. At March 31, 2015 and December 31, 2014, the Company has accrued $2.3 million and $2.9 million, respectively, for penalties.

The Company is routinely under audit by federal, state, local and foreign authorities in the area of income tax. These audits include questioning the timing and the amount of income and deductions and the allocation of income and deductions among various tax jurisdictions. The Internal Revenue Service is currently auditing the Company's federal income tax returns for the years ended December 31, 2010 through 2012. Various other jurisdictions are open to examination for various tax years beginning with 2009. Income taxes payable include reserves considered sufficient to pay assessments that may result from examination of prior year tax returns. Changes to reserves from period to period and differences between amounts paid, if any, upon resolution of audits and amounts previously provided may be material. Differences between the reserves for uncertain tax positions and the amounts owed by the Company are recorded in the period they become known.

At March 31, 2015 and December 31, 2014, unrecognized tax benefits, including interest, are $30.4 million and $33.2 million, respectively. If unrecognized tax benefits at March 31, 2015 are subsequently recognized, $28.1 million, net of related deferred tax assets and interest, would reduce income tax provision for continuing operations. The Company believes that it is reasonably possible that its unrecognized tax benefits could decrease by $7.8 million within twelve months of March 31, 2015 primarily due to expirations of statutes of limitations; $7.4 million of which would reduce the income tax provision for continuing operations.

FINANCIAL POSITION, LIQUIDITY AND CAPITAL RESOURCES

Financial Position

	March 31, 2015	December 31, 2014
	(In thousands)	
Cash and cash equivalents:		
United States [1]	$470,698	$770,050
All other countries [2]	200,899	220,355
Marketable securities (United States) [3]	205,621	160,648
Total cash and cash equivalents and marketable securities	$877,218	$1,151,053
Long-term debt:		
2013 Senior Notes due November 30, 2018	$500,000	$500,000
2012 Senior Notes due December 15, 2022	500,000	500,000
Liberty Bonds due September 1, 2035	80,000	80,000
Total long-term debt	$1,080,000	$1,080,000

[1] Domestically, cash equivalents primarily consist of commercial paper rated A2/P2 or better and AAA rated money market funds.

[2] Internationally, cash equivalents primarily consist of AAA rated money market funds and time deposits. If needed for our U.S. operations, most of the cash and cash equivalents held by the Company's foreign subsidiaries could be repatriated; however, under current law, would be subject to U.S. federal and state income taxes. We have not provided for any such tax because the Company currently does not anticipate a need to repatriate these funds to finance our U.S. operations and it is the Company's intent to indefinitely reinvest these funds outside of the U.S.

[3] Marketable securities consist of short-to-medium-term debt securities issued by investment grade corporate issuers and an equity security. The Company invests in marketable debt securities with active secondary or resale markets to ensure portfolio liquidity to fund current operations or satisfy other cash requirements as needed. The Company also invests in equity securities as part of its investment strategy.

Cash Flow Information

In summary, the Company's cash flows attributable to continuing operations are as follows:

	Three Months Ended March 31,	
	2015	2014
	(In thousands)	
Net cash (used in) provided by operating activities	$(3,810)	$42,641
Net cash used in investing activities	(65,967)	(128,568)
Net cash used in financing activities	(237,576)	(12,822)

2015

Net cash provided by operating activities attributable to continuing operations consists of earnings or loss from continuing operations adjusted for non-cash items, including stock-based compensation expense, depreciation, amortization of intangibles, asset impairment charges, excess tax benefits from stock-based awards, deferred income taxes, equity in earnings or losses of unconsolidated affiliates, acquisition-related contingent consideration fair value adjustments and the effect of changes in working capital. Net cash used in operating activities attributable to continuing operations in 2015 consists of a $49.5 million decrease in cash from changes in working capital, partially offset by earnings from continuing operations of $21.9 million and adjustments for non-cash items of $23.9 million . Adjustments for non-cash items primarily consist of $18.9 million of stock-

based compensation, $15.6 million of depreciation and $12.6 million of amortization of intangibles, partially offset by $16.8 million of excess tax benefits from stock-based awards and $7.0 million in acquisition-related contingent consideration fair value adjustments. The decrease from changes in working capital consist primarily of a decrease in income taxes payable of $41.4 million, a decrease of $33.4 million in accounts payable and other current liabilities, partially offset by an increase in deferred revenue of $23.0 million. The decrease in income taxes payable is primarily due to the payment of 2014 tax liabilities in 2015. The decrease in accounts payable and other current liabilities is due to a decrease in accrued employee compensation and benefits, a decrease in accrued revenue share and a seasonal decrease in payables to suppliers at Shoebuy, partially offset by an increase in accrued advertising expense at The Match Group. The decrease in accrued employee compensation and benefits is due to the payment of 2014 cash bonuses in 2015. The decrease in accrued revenue share is due to lower B2B revenue in the Search & Applications segment. The increase in deferred revenue is due to growth in subscription revenue at The Match Group and Vimeo, and acquisitions.

Net cash used in investing activities attributable to continuing operations in 2015 includes the purchase of marketable debt securities, net of proceeds from maturities and sales, of $41.9 million, the purchase of investments and acquisitions of $14.1 million and capital expenditures of $12.9 million, primarily related to the internal development of software to support our products and services.

Net cash used in financing activities attributable to continuing operations in 2015 includes $200.0 million for the repurchase of 3.0 million shares of common stock at an average price of $67.68 per share, $28.7 million related to the payment of cash dividends to IAC shareholders, $15.3 million for the purchase of noncontrolling interests and $10.3 million in proceeds related to the issuance of common stock, net of withholding taxes, partially offset by excess tax benefits from stock-based awards of $16.8 million.

2014

Net cash provided by operating activities attributable to continuing operations in 2014 consists of earnings from continuing operations of $34.3 million and adjustments for non-cash items of $21.9 million, partially offset by a decrease in cash from changes in working capital of $13.6 million. Adjustments for non-cash items primarily consist of $14.8 million of depreciation, $12.0 million of amortization of intangibles, $9.6 million of stock-based compensation expense, partially offset by $24.2 million of excess tax benefits from stock-based awards. The decrease from changes in working capital consists primarily of an increase in accounts receivable of $20.4 million and a decrease of $11.7 million in accounts payable and other current liabilities, partially offset by an increase in deferred revenue of $16.9 million and an increase in income taxes payable of $6.7 million. The increase in accounts receivable is primarily due to our services agreement with Google and is due to an increase in revenue in the first quarter of 2014 compared to the fourth quarter of 2013. The related receivable from Google was $128.0 million and $112.3 million at March 31, 2014 and December 31, 2013, respectively. The increase in accounts receivable was also impacted by growth in revenue at our HomeAdvisor business. The decrease in accounts payable and other current liabilities is due to a decrease in accrued employee compensation and benefits, accrued revenue share, and a seasonal decrease in payables to suppliers at Shoebuy, partially offset by an increase in accrued advertising expense at Search & Applications and The Match Group. The decrease in accrued employee compensation and benefits is due to the payment of 2013 cash bonuses in 2014. The increase in deferred revenue is primarily due to growth in subscription revenue at The Match Group and Vimeo. The increase in income taxes payable is due to current year income tax accruals in excess of current year income tax payments.

Net cash used in investing activities attributable to continuing operations in 2014 includes cash consideration used in acquisitions and investments of $85.8 million, which includes the acquisition of the ValueClick O&O website businesses, the purchase of marketable debt securities of $32.8 million and capital expenditures of $9.7 million, primarily related to the internal development of software to support our products and services.

Net cash used in financing activities attributable to continuing operations in 2014 includes $30.0 million for the purchase of noncontrolling interests and $20.0 million related to the payment of cash dividends to IAC shareholders, partially offset by excess tax benefits from stock-based awards of $24.2 million and the return of $12.4 million of funds held in escrow related to the Meetic tender offer.

Liquidity and Capital Resources

The Company's principal sources of liquidity are its cash and cash equivalents and marketable securities as well as cash flows generated from operations. The Company has a $300 million revolving credit facility, which expires on December 21, 2017, and is available as an additional source of financing. At March 31, 2015, there were no outstanding borrowings under the revolving credit facility.

The Company anticipates that it will need to make capital and other expenditures in connection with the development and expansion of its operations. The Company expects that 2015 capital expenditures will be higher than 2014. At March 31, 2015, IAC had 5.6 million shares remaining in its share repurchase authorization. IAC may purchase shares over an indefinite period of time on the open market and in privately negotiated transactions, depending on those factors IAC management deems relevant at any particular time, including, without limitation, market conditions, share price and future outlook. On April 28, 2015, IAC declared a quarterly cash dividend of $0.34 per share of common and Class B common stock outstanding payable on June 1, 2015 to stockholders of record on May 15, 2015. Future declarations of dividends are subject to the determination of IAC's Board of Directors.

The Company believes its existing cash, cash equivalents and marketable securities, together with its expected positive cash flows generated from operations and available borrowing capacity under its $300 million revolving credit facility, will be sufficient to fund its normal operating requirements, including capital expenditures, share repurchases, quarterly cash dividends, and investing and other commitments for the foreseeable future. Our liquidity could be negatively affected by a decrease in demand for our products and services. The Company may make acquisitions and investments that could reduce its cash, cash equivalents and marketable securities balances and as a result, the Company may need to raise additional capital through future debt or equity financing to provide for greater financial flexibility. Additional financing may not be available at all or on terms favorable to us. The indentures governing the 2013 and 2012 Senior Notes restrict our ability to incur additional indebtedness in the event we are not in compliance with the maximum leverage ratio of 3.0 to 1.0. In addition, the terms of the revolving credit facility require that we maintain a leverage ratio of not more than 3.0 to 1.0 and restrict our ability to incur additional indebtedness. As of March 31, 2015, the Company was in compliance with all of these covenants.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

At March 31, 2015, there have been no material changes to the Company's contractual obligations, commercial commitments and off-balance sheet arrangements since the disclosure in our Annual Report on Form 10-K for the year ended December 31, 2014.

IAC'S PRINCIPLES OF FINANCIAL REPORTING

IAC reports Adjusted EBITDA as a supplemental measure to U.S. generally accepted accounting principles ("GAAP"). This measure is one of the primary metrics by which we evaluate the performance of our businesses, on which our internal budgets are based and by which management is compensated. We believe that investors should have access to, and we are obligated to provide, the same set of tools that we use in analyzing our results. This non-GAAP measure should be considered in addition to results prepared in accordance with GAAP, but should not be considered a substitute for or superior to GAAP results. IAC endeavors to compensate for the limitations of the non-GAAP measure presented by providing the comparable GAAP measure with equal or greater prominence and descriptions of the reconciling items, including quantifying such items, to derive the non-GAAP measure. We encourage investors to examine the reconciling adjustments between the GAAP and non-GAAP measure, which we discuss below.

Definition of IAC's Non-GAAP Measure

Adjusted EBITDA is defined as operating income excluding: (1) stock-based compensation expense; (2) depreciation; and (3) acquisition-related items consisting of (i) amortization of intangible assets and goodwill and intangible asset impairments and (ii) gains and losses recognized on changes in the fair value of contingent consideration arrangements. We believe this measure is useful for analysts and investors as this measure allows a more meaningful comparison between our performance and that of our competitors. Moreover, our management uses this measure internally to evaluate the performance of our business as a whole and our individual business segments. The above items are excluded from our Adjusted EBITDA measure because these items are non-cash in nature, and we believe that by excluding these items, Adjusted EBITDA corresponds more closely to the cash operating income generated from our business, from which capital investments are made and debt is serviced. Adjusted EBITDA has certain limitations in that it does not take into account the impact to IAC's statement of operations of certain expenses.

Non-Cash Expenses That Are Excluded From IAC's Non-GAAP Measure

Stock-based compensation expense consists principally of expense associated with the grants, including unvested grants assumed in acquisitions, of stock options, restricted stock units ("RSUs") and performance-based RSUs. These expenses are not paid in cash, and we include the related shares in our fully diluted shares outstanding using the treasury stock method; however, performance-based RSUs are included only to the extent the performance criteria have been met (assuming the end of the reporting period is the end of the contingency period). Upon the exercise of certain stock options and vesting of RSUs and performance-based RSUs, the awards are settled, at the Company's discretion, on a net basis, with the Company remitting the required tax-withholding amount from its current funds.
Depreciation is a non-cash expense relating to our property and equipment and is computed using the straight-line method to allocate the cost of depreciable assets to operations over their estimated useful lives.
Amortization of intangible assets and goodwill and intangible asset impairments are non-cash expenses relating primarily to acquisitions. At the time of an acquisition, the identifiable definite-lived intangible assets of the acquired company, such as content, technology, customer lists, advertiser and supplier relationships, are valued and amortized over their estimated lives. Value is also assigned to acquired indefinite-lived intangible assets, which comprise trade names and trademarks, and goodwill that are not subject to amortization. An impairment is recorded when the carrying value of an intangible asset or goodwill exceeds its fair value. While it is likely that we will have significant intangible amortization expense as we continue to acquire companies, we believe that intangible assets represent costs incurred by the acquired company to build value prior to acquisition and the related amortization and impairment charges of intangible assets or goodwill, if applicable, are not ongoing costs of doing business.
Gains and losses recognized on changes in the fair value of contingent consideration arrangements are accounting adjustments to report contingent consideration liabilities at fair value. These adjustments can be highly variable and are excluded from our assessment of performance because they are considered non-operational in nature and, therefore, are not indicative of current or future performance or ongoing costs of doing business.

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RECONCILIATION OF ADJUSTED EBITDA

For a reconciliation of Adjusted EBITDA to operating income (loss) by reportable segment for the three months ended March 31, 2015 and 2014, see Note 8 to the consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

At March 31, 2015, there have been no material changes to the Company's instruments or positions that are sensitive to interest rate risk and equity price risk since the disclosure in our Annual Report on Form 10-K for the year ended December 31, 2014.

Foreign Currency Exchange Risk

The Company conducts business in certain foreign markets, primarily in the European Union. For the three months ended March 31, 2015, international revenue accounted for 26% of consolidated revenue. The Company's primary exposure to foreign currency exchange risk relates to investments in foreign subsidiaries that transact business in a functional currency other than the U.S. Dollar, primarily the Euro. As foreign currency exchange rates change, translation of the statements of operations of the Company's international businesses into U.S. dollars affects year-over-year comparability of operating results. The average Euro versus the U.S. Dollar exchange rate was 18% lower in the first quarter of 2015 than 2014. The decrease had a significant impact to the revenue of The Match Group. The Match Group revenue, Dating revenue and Dating International revenue would have increased approximately 19%, 8% and 9%, respectively, as compared to the reported increases of 13% and 2% and a decrease of 8%, respectively, had the foreign currency exchange rates been the same as the first quarter of 2014.

Historically, the Company has not hedged any foreign currency exposures. Our continued international expansion increases our exposure to exchange rate fluctuations and as a result such fluctuations could have a significant impact on our future results of operations.

Item 4. Controls and Procedures

The Company monitors and evaluates on an ongoing basis its disclosure controls and internal control over financial reporting in order to improve its overall effectiveness. In the course of these evaluations, the Company modifies and refines its internal processes as conditions warrant.

As required by Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), IAC management, including the Chairman and Senior Executive and the Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures as defined by Rule 13a-15(e) and 15d-15(e) under the Exchange Act. Based on this evaluation, the Chairman and Senior Executive and the Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report in providing reasonable assurance that information we are required to disclose in our filings with the Securities and Exchange Commission under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and Forms, and include controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

As required by Rule 13a-15(d) of the Exchange Act, the Company, under the supervision and with the participation of IAC management, including the Chairman and Senior Executive and the Chief Financial Officer, also evaluated whether any changes occurred to the Company's internal control over financial reporting during the period covered by this report that have materially affected, or are reasonably likely to materially affect, such control. Based on that evaluation, the Company concluded that there has been no such change during the period covered by this report.

PART II
OTHER INFORMATION
Item 1A. Risk Factors

Cautionary Statement Regarding Forward-Looking Information

This quarterly report on Form 10-Q contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. The use of words such as "anticipates," "estimates," "expects," "intends," "plans" and "believes," among others, generally identify forward-looking statements. These forward-looking statements include, among others, statements relating to: IAC's future financial performance, IAC's business prospects and strategy, anticipated trends and prospects in the industries in which IAC's businesses operate and other similar matters. These forward-looking statements are based on IAC management's current expectations and assumptions about future events, which are inherently subject to uncertainties, risks and changes in circumstances that are difficult to predict.

Actual results could differ materially from those contained in these forward-looking statements for a variety of reasons, including, among others: changes in senior management at IAC and/or its businesses, changes in our relationship with, or policies implemented by, Google, adverse changes in economic conditions, either generally or in any of the markets or industries in which IAC's businesses operate, adverse trends in the online advertising industry or the advertising industry generally, our ability to convert visitors to our various websites into users and customers, our ability to offer new or alternative products and services in a cost-effective manner and consumer acceptance of these products and services, changes in industry standards and technology, actual tax liabilities that differ materially from our estimates, operational and financial risks relating to acquisitions, our ability to expand successfully into international markets and regulatory changes. Certain of these and other risks and uncertainties are discussed in IAC's filings with the SEC, including in Part I "Item 1A. Risk Factors" of our annual report on Form 10-K for the fiscal year ended December 31, 2014. Other unknown or unpredictable factors that could also adversely affect IAC's business, financial condition and operating results may arise from time to time. In light of these risks and uncertainties, the forward-looking statements discussed in this report may not prove to be accurate. Accordingly, you should not place undue reliance on these forward-looking statements, which only reflect the views of IAC management as of the date of this quarterly report. IAC does not undertake to update these forward-looking statements.

Risk Factors

In addition to the other information set forth in this quarterly report, you should carefully consider the risk factors discussed in Part I "Item 1A. Risk Factors" of our annual report on Form 10-K for the fiscal year ended December 31, 2014, which could materially affect our business, financial condition or future operating results. The risks described in this report are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or future operating results.
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

The following table sets forth purchases by the Company of its common stock during the quarter ended March 31, 2015:

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid Per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs[1]	(d) Maximum Number of Shares that May Yet Be Purchased Under Publicly Announced Plans or Programs
January 2015	—	$—	—	8,562,170
February 2015	1,119,483	$66.03	1,119,483	7,442,687
March 2015	1,835,783	$68.68	1,835,783	5,606,904[2]
Total	2,955,266	$67.68	2,955,266	5,606,904[2]

(1) Reflects repurchases made pursuant to the repurchase authorization previously announced in April 2013.

(2) Represents the total number of shares of common stock that remained available for repurchase as of March 31, 2015 pursuant to the April 2013 repurchase authorization. IAC may purchase shares pursuant to this repurchase authorization over an indefinite period of time in the open market and/or privately negotiated transactions, depending on those factors IAC management deems relevant at any particular time, including, without limitation, market conditions, share price and future outlook.

Item 6. Exhibits

The documents set forth below, numbered in accordance with Item 601 of Regulation S-K, are filed herewith, incorporated by reference to the location indicated or furnished herewith.

Exhibit Number	Description	Location
3.1	Restated Certificate of Incorporation of IAC/InterActiveCorp.	Exhibit 3.1 to the Registrant's Registration Statement on Form 8-A/A, filed on August 12, 2005.
3.2	Certificate of Amendment of the Restated Certificate of Incorporation of IAC/InterActiveCorp.	Exhibit 3.1 to the Registrant's Current Report on Form 8-K, filed on August 22, 2008.
3.3	Amended and Restated By-Laws of IAC/InterActiveCorp.	Exhibit 3.1 to the Registrant's Current Report on Form 8-K, filed on December 6, 2010.
31.1	Certification of the Chairman and Senior Executive pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act.(1)	
31.2	Certification of the Executive Vice President and Chief Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act.(1)	
32.1	Certification of the Chairman and Senior Executive pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act.(2)	
32.2	Certification of the Executive Vice President and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act.(2)	
101.INS	XBRL Instance	
101.SCH	XBRL Taxonomy Extension Schema	
101.CAL	XBRL Taxonomy Extension Calculation	
101.DEF	XBRL Taxonomy Extension Definition	
101.LAB	XBRL Taxonomy Extension Labels	
101.PRE	XBRL Taxonomy Extension Presentation	

(1) Filed herewith.

(2) Furnished herewith.

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.

Dated: May 1, 2015

IAC/INTERACTIVECORP

By: /s/ JEFFREY W. KIP
Jeffrey W. Kip
Executive Vice President and
Chief Financial Officer

Signature	Title	Date
/s/ JEFFREY W. KIP Jeffrey W. Kip	Executive Vice President and Chief Financial Officer	May 1, 2015

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