

FLAGSTAR BANCORP INC

Form DEF 14A

April 24, 2006

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
SCHEDULE 14A**

**Proxy Statement Pursuant to Section 14(a) of the Securities  
Exchange Act of 1934 (Amendment No.     )**

Filed by the Registrant ☐

Filed by a Party other than the Registrant ☐

Check the appropriate box:

☐ Preliminary Proxy Statement

☐ Confidential, For Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

☒ Definitive Proxy Statement

☐ Definitive Additional Materials

☐ Soliciting Material Pursuant to §240.14a-12

**Flagstar Bancorp, Inc.**

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

☒ No fee required.

☐ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

- 1) Title of each class of securities to which transaction applies:
  - 2) Aggregate number of securities to which transaction applies:
  - 3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):
  - 4) Proposed maximum aggregate value of transaction:
  - 5) Total fee paid:
- ☐ Fee paid previously with preliminary materials.
- ☐ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration

statement number, or the Form or Schedule and the date of its filing.

- 1) Amount Previously Paid:
  - 2) Form, Schedule or Registration Statement No.:
  - 3) Filing Party:
  - 4) Date Filed:
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April 24, 2006

To our stockholders:

We invite you to attend the 2006 Annual Meeting of Stockholders of Flagstar Bancorp, Inc. to be held at the national headquarters of the Company, 5151 Corporate Dr., Troy, Michigan on Friday, May 26, 2006 at 1:00 p.m., local time. Enclosed are a notice setting forth the business expected to come before the Annual Meeting, the Proxy Statement, the Proxy card, and a copy of our Annual Report to Stockholders for 2005. Our directors and officers as well as representatives of Virchow, Krause & Company, LLP, our independent auditors for 2005, will be present to respond to questions that you may have.

Your vote is very important to us. On behalf of the Board of Directors, we urge you to sign, date and return the enclosed proxy as soon as possible, even if you currently plan to attend the Annual Meeting. This will not prevent you from voting in person, but will assure that your vote is counted if you are unable to attend the Annual Meeting.

Thank you for your continuing support.

Sincerely,

/s/ Thomas J. Hammond

Thomas J. Hammond  
*Chairman of the Board*

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FLAGSTAR BANCORP, INC.  
5151 CORPORATE DR.  
TROY, MI 48098  
(248) 312-2000

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS  
TO BE HELD ON MAY 26, 2006

**NOTICE IS HEREBY GIVEN** that the 2006 Annual Meeting of Stockholders (the "Annual Meeting") of Flagstar Bancorp, Inc. (the "Company") will be held on Friday, May 26, 2006 at 1:00 p.m., local time, at the national headquarters of the Company, 5151 Corporate Dr., Troy, Michigan.

A proxy card and a proxy statement for the Annual Meeting are enclosed. We are also enclosing a copy of our 2005 Annual Report to Stockholders.

The Annual Meeting is for the purpose of considering and acting upon the following matters:

1. to elect six directors to the Board of Directors to hold office for a term of two years and until their successors shall have been duly elected and qualified;
2. to ratify the appointment of Virchow, Krause & Company, LLP as the Company's independent auditors for the year ending December 31, 2006;
3. to amend and restate the Second Restated Articles of Incorporation to eliminate supermajority voting requirements;
4. to amend and restate the Second Restated Articles of Incorporation to provide that the term of directors appointed to fill a vacancy will expire at the next annual meeting of stockholders;
5. to adopt the 2006 Equity Incentive Plan; and
6. to transact such other business as may properly come before the Annual Meeting or any adjournments thereof.

NOTE: The Board of Directors is not aware of any other business to come before the Annual Meeting.

Any action may be taken on any one of the foregoing proposals at the Annual Meeting on the date specified above or on any date or dates to which, by original or later adjournments, the Annual Meeting may be adjourned. Stockholders of record on April 12, 2006, will be entitled to notice of and vote at the Annual Meeting and any adjournments thereof. A complete list of stockholders entitled to vote will be available for inspection at the Annual Meeting.

You are requested to fill in and sign the enclosed form of proxy, which is solicited by the Board of Directors and to mail it promptly in the enclosed envelope. The proxy will not be used if you attend and choose to vote in person at the Annual Meeting.

BY ORDER OF THE BOARD OF DIRECTORS

/s/ Mary Kay Ruedisueli

Mary Kay Ruedisueli  
Secretary

Troy, Michigan  
April 24, 2006

It is important that proxies be returned promptly. Therefore, whether or not you plan to be present in person at the Annual Meeting, please sign, date, and complete the enclosed proxy card and return it in the enclosed envelope. No postage is required if mailed in the United States.

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PROXY STATEMENT  
OF  
FLAGSTAR BANCORP, INC.  
5151 CORPORATE DR.  
TROY, MI 48098  
(248) 312-2000

ANNUAL MEETING OF STOCKHOLDERS  
MAY 26, 2006

**This Proxy Statement and the enclosed Proxy Card are furnished in connection with the solicitation of proxies by the Board of Directors (the Board) of Flagstar Bancorp, Inc. (the Company). They will be used at the 2006 Annual Meeting of Stockholders of the Company (the Annual Meeting), that will be held on Friday, May 26, 2006 at 1:00 p.m., local time, at the national headquarters of the Company and Flagstar Bank, fsb (the Bank), 5151 Corporate Dr., Troy, Michigan. The accompanying Notice of Annual Meeting, this Proxy Statement, and the Proxy Card are being first mailed to stockholders entitled to vote at the Annual Meeting on or about April 24, 2006.**

**QUESTIONS AND ANSWERS**

**Why am I receiving these materials?**

The Board is providing these proxy materials to you in connection with the Annual Meeting, to be held on May 26, 2006. As a stockholder, you are invited to attend the Annual Meeting, and are entitled and requested to vote on the items of business described in this Proxy Statement. Directors and officers of the Company as well as representatives of Virchow, Krause & Company, LLP, the Company's independent auditor for 2005, will be present to respond to questions that you may have.

**What information is contained in this Proxy Statement?**

This information relates to the proposals to be voted on at the Annual Meeting, the voting process, compensation of the Company's directors and most highly paid executives, and certain other information required to be disclosed in this Proxy Statement.

**Who is soliciting my vote pursuant to this Proxy Statement?**

The Board is soliciting your vote at the 2006 Annual Meeting.

**Who is entitled to vote?**

Only stockholders of record at the close of business on April 12, 2006 (the Record Date) will be entitled to notice of and vote at the Annual Meeting.

**How many shares are eligible to be voted?**

As of the Record Date, the Company had 63,488,777 shares of common stock (Common Stock) outstanding. Each outstanding share of Common Stock will entitle its holder to one vote on each matter to be voted on at the Annual Meeting. For information regarding security ownership by the beneficial owners of more than 5% of the Common Stock and by management, see SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS and SECURITY OWNERSHIP OF MANAGEMENT.

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### **What am I voting on?**

You are voting on each of the following matters:

1. to elect six directors to the Board. The Company's nominees are Thomas J. Hammond, Kirsten A. Hammond, Charles Bazy, Michael Lucci, Sr., Robert W. Dewitt, and Frank D. Angelo. All are current Company directors, and each will have a term of two years. No other nominations have been received.
2. to ratify the appointment of Virchow, Krause & Company, LLP as the Company's independent auditors for the year ending December 31, 2006.
3. to amend and restate the Second Restated Articles of Incorporation to eliminate supermajority voting requirements.
4. to amend and restate the Second Restated Articles of Incorporation to provide that the term of directors appointed to fill a vacancy will expire at the next annual meeting of stockholders.
5. to adopt the 2006 Equity Incentive Plan.

You will also be entitled to vote on any other business that properly comes before the Annual Meeting or any adjournments thereof.

### **How does the Board recommend that I vote?**

The Board recommends that you vote FOR each director nominee, FOR the ratification of Virchow, Krause & Company, LLP as our independent auditor, FOR the proposed amendment to and the restatement of the Second Restated Articles of Incorporation to eliminate supermajority voting requirements, FOR the proposed amendment to and restatement of the Second Restated Articles of Incorporation to provide that terms of directors appointed to fill a vacancy will expire at the next annual meeting of stockholders, and FOR adoption of the 2006 Equity Incentive Plan.

### **How many votes are required to hold the Annual Meeting and what are the voting procedures?**

**Quorum Requirement:** Michigan law provides that a quorum be present to allow any stockholder action at a meeting. A quorum consists of a majority of all of the outstanding shares of Common Stock that are entitled to vote at the Annual Meeting. Therefore, at the Annual Meeting, the presence, in person or by proxy, of the holders of at least 31,744,389 shares of Common Stock will be required to establish a quorum. Stockholders of record who are present at the Annual Meeting in person or by proxy but who abstain from voting are still counted towards the establishment of a quorum. This will include brokers holding customers' shares of record even though they may abstain from certain votes.

**Required Votes:** Each outstanding share of Common Stock is entitled to one vote on each proposal at the Annual Meeting. The number of required votes set forth below assumes that a quorum is present at the Annual Meeting.

1. *Election of Directors.* The six nominees who receive the greatest number of votes cast for directors will be elected. There is no cumulative voting allowed for Company directors.
2. *Ratification of Independent Auditor.* The action will be approved if greater than a majority of shares represented at the Annual Meeting, either in person or by proxy, and entitled to vote are cast for it.
3. *Elimination of Supermajority Voting Requirements.* The action will be approved if greater than a majority of shares of Common Stock outstanding as of the Record Date are cast for it.
4. *Term of Directors Appointed to Fill Vacancies by the Board.* The action will be approved if greater than a majority of shares of Common Stock outstanding as of the Record Date are cast for it.

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5. *Adoption of 2006 Equity Incentive Plan.* The action will be approved if greater than a majority of shares represented at the Annual Meeting, either in person or by proxy, and entitled to vote are cast for it.

With respect to the election of directors, failure to vote, abstentions and broker non-votes will have no impact.

With respect to the two proposed amendments to and the restatement of the Second Restated Articles of Incorporation, failure to vote, abstentions and broker non-votes for a proposal will have the same effect as voting against that proposal. With respect to the adoption of the 2006 Equity Incentive Plan and the ratification of our independent auditor, failure to vote, abstentions and broker non-votes will have no effect because these shares will not be considered shares entitled to vote and therefore will not be counted as votes for or against the proposals.

**What is a broker non-vote?**

If you hold your shares in street name through a broker or other nominee, whether the broker may vote your shares in its discretion depends on the proposals before the meeting. Under the rules of the New York Stock Exchange, your broker may vote your shares in its discretion on routine matters. Proposals that are not considered routine cannot be voted unless you specifically instruct your brokers. Accordingly, if your broker has not received your voting instructions with respect to that proposal, your broker cannot vote your shares on that proposal. This is referred to as a broker non-vote.

**How may I cast my vote?**

If you are the stockholder of record: You may vote by one of the following two methods (as instructed on the enclosed proxy card):

1. in person at the Annual Meeting, or
2. by mail.

Whichever method you use, the proxies identified on the back of the proxy card will vote the shares of which you are the stockholder of record in accordance with your instructions. If you submit a proxy card without giving specific voting instructions, the proxies will vote the shares as recommended by the Board of Directors.

If you own your shares in street name, that is, through a brokerage account or in another nominee form: You must provide instructions to the broker or nominee as to how your shares should be voted. Your broker or nominee will usually provide you with the appropriate instruction forms at the time you receive this Proxy Statement and the Company's Annual Report. If you own your shares in this manner, you cannot vote in person at the Annual Meeting unless you receive a proxy to do so from the broker or the nominee, and you bring the proxy to the Annual Meeting.

**How may I revoke or change my vote?**

If you are the record owner of your shares, you may revoke your proxy at any time before it is voted at the Annual Meeting by:

1. submitting a new proxy card bearing a later date,
2. delivering written notice to the Secretary of the Company prior to May 26, 2006, stating that you are revoking your proxy, or
3. attending the Annual Meeting and voting your shares in person.

Please note that your attendance at the Annual Meeting will not, by itself, constitute revocation of your proxy.

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**Who is paying for the costs of this proxy solicitation?**

The Company will bear the cost of preparing, printing and mailing the materials in connection with this solicitation of proxies. In addition to mailing these materials, officers and regular employees of the Company may, without being additionally compensated, solicit proxies personally and by mail, telephone, facsimile or electronic communication. The Company will reimburse banks and brokers for their reasonable out-of-pocket expenses related to forwarding proxy materials to beneficial owners of stock or otherwise in connection with this solicitation.

**Who will count the votes?**

Matthew I. Roslin and Mary Kay Ruedisueli, the Company's inspectors of election for the Annual Meeting, will receive and tabulate the ballots and voting instruction forms.

**What happens if the Annual Meeting is postponed or adjourned?**

Your proxy will still be effective and may be voted at the postponed meeting. You will still be able to change or revoke your proxy until it is voted.

**What happens if a nominee is unable to serve, new business is introduced or procedural matters are voted upon?**

Your proxy confers discretionary authority on the persons named therein to vote with respect to the election of any person or a director where the nominee is unable to serve or for good cause will not serve, with respect to matters incident to the conduct of the Annual Meeting and with respect to any other matter presented to the Annual Meeting if notice of such matter has not been delivered to the Company in accordance with the Second Restated Articles of Incorporation. For more information on submitting matters to the Company, see STOCKHOLDER MATTERS herein. If any other matters are properly brought before the Annual Meeting, the persons named in the proxy will vote the shares represented by such proxies on such matters as determined by a majority of the Board. Except for procedural matters incident to the conduct of the Annual Meeting, the Company does not know of any other matters that are to come before the Annual Meeting.

**PROPOSAL I  
ELECTION OF DIRECTORS**

The Board is currently composed of twelve directors. At this Annual Meeting, the terms of six of the current directors—Thomas J. Hammond, Kirstin A. Hammond, Charles Bazy, Michael Lucci, Sr., Robert W. DeWitt, and Frank D. Angelo—will expire. The Board has nominated each of them to serve for a new two-year term and until their respective successors are duly elected and qualified.

It is intended that the persons named in the proxies solicited by the Board will vote for the election of each of these nominees. If the nominee is unable to serve, the shares represented by all properly executed proxies which have not been revoked will be voted for the election of such substitute as the Board may recommend, or the size of the Board may be reduced to eliminate the vacancy. At this time, the Board does not know of any reason why any nominee might be unable to serve.

**The Board of Directors recommends a vote FOR election as directors of all of the nominees listed below.**

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The following table sets forth, for the nominees and each continuing director, his or her name, that person's age as of the Record Date, the year he or she first became a director of the Company and the expiration of his or her current term. Each of the nominees listed below has consented to serve if elected.

Name	Age as of the Record Date	Year First Elected Director of the Company	Current Term To Expire
Board Nominees for Terms to Expire in 2008			
Thomas J. Hammond	62	1993	2006
Kirstin A. Hammond	40	2002	2006
Charles Bazy	76	2002	2006
Michael Lucci, Sr.	66	2004	2006
Robert W. DeWitt	66	2004	2006
Frank D. Angelo	62	2004	2006
Directors Continuing in Office			
Mark T. Hammond	40	1993	2007
Robert O. Rondeau, Jr.	40	2002	2007
James D. Coleman	59	1993	2007
Richard S. Elsea	76	1997	2007
B. Brian Tauber	40	2005	2007
Jay J. Hansen	42	2005	2007

The following sets forth the business experience of each director of the Company.

**Thomas J. Hammond** has served as Chairman of the Board of Directors of the Company since 1993, and served as President from 1993 through 1995 and Chief Executive Officer from 1993 through 2002. Mr. Hammond founded the Bank in 1987 and has served as Chairman of its Board of Directors since that time. Mr. Hammond is the father of Mark T. Hammond, President, Chief Executive Officer and Vice Chairman of the Board of Directors, and is the father-in-law of Kirstin A. Hammond and Robert O. Rondeau, Jr., each of whom is an Executive Director of the Company and the Bank and a member of the Board of Directors of the Company.

**Mark T. Hammond** has served as Vice Chairman of the Board of Directors of the Company and of the Bank since 1993, as President of the Company and the Bank since 1995, and as Chief Executive Officer of the Company and the Bank since 2002. Prior to being named President, Mr. Hammond was a Senior Vice President responsible for sales and secondary marketing and served in various other positions in the Bank since 1987. Mr. Hammond is a graduate of the Wharton School of Business (University of Pennsylvania), where he received a Bachelor's Degree in 1987, and has served on the President's Advisory Board of Fannie Mae. Mr. Hammond is the son of Thomas J. Hammond, the husband of Kirstin A. Hammond, and the brother-in-law of Robert O. Rondeau, Jr.

**Charles Bazy** has served as a Member of the Board of Directors of the Company since 2002 and of the Bank since 1987. Following his retirement in 1988 from Ford Motor Company, where he served as a product development manager for 33 years, Mr. Bazy founded and is President of Charles Bazy & Associates, a sales and marketing organization based in Michigan.

**Dr. James D. Coleman** has served as a Member of the Board of Directors of the Company since 1993 and of the Bank since 1987. He is a board certified physician who owned and operated several Emergency Room Staffing Companies prior to his retirement in 1997.

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**Frank D. Angelo** has served as a Member of the Board of Directors of the Company since 2004. Mr. D. Angelo is the President of Century 21 Hartford South, Inc., a Michigan-based real estate sales organization that he founded in 1972.

**Robert W. DeWitt** has served as a Member of the Board of Directors of the Company and of the Bank since 2004. Mr. DeWitt is the President of DeWitt Building Co, a Michigan-based builder of custom homes and remodeling projects that he founded in 1979. Mr. DeWitt has been in the home building and remodeling business for 42 years.

**Richard S. Elsea** has served as a Member of the Board of Directors of the Company and of the Bank since 1997. Mr. Elsea has been President since 1970 of Real Estate One, a company founded in 1929, and which is Michigan's largest real estate sales organization. Mr. Elsea also serves on the Board of Directors of Providence Hospital, a Michigan based not-for-profit organization.

**Jay J. Hansen** was appointed to the Board in 2005. Mr. Hansen was, in February 2006, promoted to Chief Operating Officer of Noble International, Ltd., a Nasdaq-listed company and a supplier of automotive parts, component assemblies and value-added services to the automotive industry, where he served as Vice President and Chief Financial Officer from May 2003 to February 2006 and as Vice President of Corporate Development from 2002 to 2003. Prior to joining Noble, Mr. Hansen was Vice President at Oxford Investment Group, a privately held merchant bank with holdings in a variety of business segments, from 1994 to 2002. Mr. Hansen is a graduate of the Wharton School of Business (University of Pennsylvania), where he received a Bachelor's Degree in 1985.

**Kirstin A. Hammond** has served as a Member of the Board of Directors of the Company since 2002. She also serves as an Executive Director of the Company and the Bank where she has been employed since 1991. Prior to joining the Bank, Ms. Hammond worked as an Investment Analyst at Manufacturer's National Bank from 1987 to 1991. Ms. Hammond graduated from the University of Michigan with a Masters degree in Business Administration in 1991 and from the Wharton School of Business (University of Pennsylvania) with a Bachelor's Degree in 1987. Ms. Hammond is the wife of Mark T. Hammond, the daughter-in-law of Thomas J. Hammond, and the sister-in-law of Robert O. Rondeau, Jr.

**Michael Lucci, Sr.** has served as a Member of the Board of Directors of the Company since 2004. Mr. Lucci retired from his position as the President and Chief Operating Officer of Bally's Total Fitness Corporation in 1996, and is currently a managing partner of Venture Contracting, a Michigan-based construction company which he founded in 1997, and Michigan Multi-King, a Michigan-based owner and operator of fast food franchises which he founded in 1980.

**Robert O. Rondeau, Jr.** has served as a Member of the Board of Directors of the Company since 2002. He also serves as an Executive Director of the Company and the Bank, where he has been employed since 1995. Prior to joining the Bank, Mr. Rondeau received a Masters degree in Business Administration from Michigan State University in 1996 and a Bachelor's Degree from Northwestern University in 1987. Mr. Rondeau is the son-in-law of Thomas J. Hammond and the brother-in-law of Mark T. Hammond and Kirstin A. Hammond.

**B. Brian Tauber** was appointed to the Board in 2005. Mr. Tauber has served as Chief Executive Officer and President of Carolina Precision Plastics, LLC, an injection molder and assembler located in Ashboro, North Carolina, since 2001. Since 2003, Mr. Tauber has also served as President and Chief Executive Officer of C Enterprises, L.P., a custom cable assembly manufacturer located in Vista, California serving the data and telecom industries. Mr. Tauber is also a principal of BLT Ventures, LLC, which acquires majority interests in mid-market manufacturing companies. Mr. Tauber received his Masters degree in Business Administration and law degree from the University of Michigan in 1992, and his undergraduate degree from the University of Pennsylvania in 1988.

### **Board and Committee Meetings and Committees**

The Board generally meets on a monthly basis, or as needed. During the year ended December 31, 2005, the Board met twelve times. No director attended fewer than 75% of the aggregate of (i) the total

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number of meetings of the Board during 2005, and (ii) the total number of meetings held by all committees of the Board on which that director served, except that B. Brian Tauber attended 67% as a result of obligations to which he committed prior to his appointment to the Board on June 21, 2005.

While the Company does not have a policy regarding director attendance at the annual meeting of stockholders, the Company encourages directors to attend every annual meeting. Ten out of eleven of the Company's directors attended the annual meeting of stockholders held on May 27, 2005.

**Nominating/ Corporate Governance Committee**

The Nominating/ Corporate Governance Committee consists of directors Robert W. DeWitt and James D. Coleman, each of whom is independent as required and defined by the New York Stock Exchange. The chairman of the Nominating/ Corporate Governance Committee is Mr. DeWitt. The Nominating/ Corporate Governance Committee met five times in 2005.

Among other things, the Nominating/ Corporate Governance Committee is responsible for reviewing with the Board annually the requisite skills and characteristics required of Board members, selecting, evaluating and recommending nominees for election by the Company's stockholders and reviewing and assessing the adequacy of the Company's policies and practices on corporate governance, including the Corporate Governance Guidelines which may be found on our website at [www.flagstar.com](http://www.flagstar.com).

The Nominating/ Corporate Governance Committee will consider prospective nominees for the Board based on the need to fill vacancies or the Board's determination to expand the size of the Board. This initial determination is based on information provided to the Committee with the recommendation of the prospective candidate, as well as the Committee's own knowledge of the prospective candidate, which may be supplemented by inquiries to the person making the recommendation. The Committee then evaluates the prospective nominee against the standards and qualifications set forth below, including relevant experience, industry expertise, intelligence, independence, diversity of background and outside commitments.

The general criteria for nomination to the Board include the following:.

Directors should possess personal and professional ethics, integrity and values, and be committed to representing the long-term interests of the Company's stockholders and other constituencies.

Directors should have reputations, both personal and professional, consistent with the image and reputation of the Company.

Each director should have relevant experience and expertise and be able to add value and offer advice and guidance to the Chief Executive Officer based on that experience and expertise.

Directors should have current knowledge and contacts in the Company's industry and other industries relevant to the Company's business, ability to work with others as an effective group and ability to commit adequate time as a director.

A majority of directors on the Board should be independent, not only as that term may be legally defined, but also without the appearance of any conflict in serving as a director. In addition, directors should be independent of any particular constituency and be able to represent the interests of the Company's stockholders and other constituencies.

Each director should have the ability to exercise sound business judgment.

Directors should be selected so that the Board of Directors is a diverse body reflecting gender, ethnic background, professional experience, current responsibilities and community involvement.

In considering director nominees, the Nominating/ Corporate Governance Committee has not used third party search firms to assist in this purpose. The Nominating/ Corporate Governance Committee recommends to the Board

the slate of directors to be nominated for election at the annual meeting of

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stockholders. The Board is responsible for making interim appointments of directors in accordance with the Company's Second Restated Articles of Incorporation and Amended and Restated Bylaws.

**Compensation Committee**

During 2005, the Compensation Committee consisted of directors James D. Coleman, Frank D. Angelo, and Robert W. DeWitt. The Compensation Committee met seven times in 2005. The Compensation Committee meets periodically to establish policies that govern executive compensation. The Compensation Committee recommends to the Board components and structure of the compensation plans for executive officers of the Company and determines and approves compensation for the Chief Executive Officer.

**Audit Committee**

The Audit Committee consists of directors Charles Bazy, Richard S. Elsea, Jay J. Hansen, and B. Brian Tauber. The chairman of the Audit Committee is Mr. Hansen. The Audit Committee met ten times in 2005. The Board has determined that Mr. Hansen qualifies as an audit committee financial expert, as defined by the rules and regulations of the SEC and that Messrs. Bazy and Tauber also qualify. Further, the Board certifies that each member of the Audit Committee is financially literate and has accounting or related financial management expertise, as such qualifications are defined by the rules of the NYSE.

The Audit Committee is responsible for reviewing the Company's audit programs and the activity of the Bank. The Audit Committee oversees the quarterly regulatory reporting process, oversees the internal compliance audits as necessary, receives and reviews the results of each external audit, reviews management's responses to auditors recommendations, and reviews management's reports on cases of financial misconduct by employees, officers or directors. The Audit Committee is also responsible for engaging the Company's independent auditor and for the compensation and oversight of the work of the independent auditor for the purpose of preparing or issuing an audit report or related work or performing other audit, review or attest services for the Company.

The Audit Committee has adopted the Flagstar Bancorp, Inc. Audit Committee Pre-Approval Policy (the Pre-Approval Policy), which requires the committee to pre-approve the audit and non-audit services performed by the independent auditor and confirm that such services do not impair the auditor's independence. Among other things, the Pre-Approval Policy provides that unless a service to be provided by the independent auditor has received general pre-approval, it requires specific pre-approval by the Audit Committee. Further, the Pre-Approval Policy provides that any services exceeding pre-approval cost levels will require specific pre-approval by the Audit Committee. In 2005, all of the fees paid to our independent auditor were pre-approved by the Audit Committee.

**Director Compensation**

The Company's general policy is to provide non-management directors with both cash and equity-based compensation that is intended to assist the Company in attracting and retaining qualified non-management directors. The Company does not pay director compensation to its directors who are also employees of the Company.

The Nominating/ Corporate Governance Committee, which consists solely of independent directors, has the primary responsibility to review director compensation and benefits on an annual basis and recommend any revisions to the Board. Non-management directors receive the following compensation for their service on the Board and its committees:

For each monthly Board meeting, \$2,500 for attendance in person and \$1,250 for attendance by telephone;

For each special telephone Board meeting, \$500;



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For each Audit Committee meeting, \$1,500 (\$2,500 for the chairman of the Audit Committee) for attendance in person and \$750 for attendance by telephone;

For each special out of office Audit Committee meeting, \$500;

For each special telephone Audit Committee meeting, \$300;

For each Compensation Committee meeting, \$600

For each telephone Compensation Committee meeting, \$300;

For each Nominating/ Corporate Governance Committee meeting, \$300 for attendance in person and \$200 for attendance by telephone;

For each meeting of non-management directors held the same day as the Board meeting, \$300 for attendance in person and \$150 for attendance by telephone; and

For each meeting of non-management directors not held the same day as the Board meeting, \$800 for attendance in person and \$300 for attendance by telephone.

The Company reimburses non-management directors that attend meetings of the Board or its committees from out-of-town for travel expenses, including accommodations, of up to \$5,000 per year.

In addition, non-management directors are eligible to receive equity-based compensation under the 1997 Employees and Directors Stock Option Plan and the 2000 Stock Incentive Plan. If PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is approved by stockholders, non-management directors will be eligible to receive equity-based compensation under the 2006 Equity Compensation Plan.

The table below details the compensation earned by the Company's non-management directors in 2005.

Non-Management Directors	Total Compensation (1)	Board Fees	Committee Fees (2)	Stock Option Grant (3)
Charles Bazzy	\$ 51,645	\$ 30,000	\$ 17,100	\$ 4,545
James D. Coleman	36,145	25,000	6,600	4,545
Richard S. Elsea	41,645	30,000	7,100	4,545
Michael Lucci, Sr.	37,245	30,000	2,700	4,545
Frank D. Angelo	39,645	30,000	5,100	4,545
Robert DeWitt	40,945	30,000	6,400	4,545
B. Brian Tauber (4)	15,880	10,000	2,700	3,180
Jay J. Hansen (5)	15,380	7,500	4,700	3,180

- (1) Consists of a sum of the compensation amounts that are reflected in this table.
- (2) Includes meetings of the Audit Committee, Compensation Committee, Nominating/ Corporate Governance Committee, and the non-management directors.
- (3) Each non-management director received a grant of 1,500 stock options in May 2005, except that Messrs. Tauber and Hansen received grants in December 2005. The amount shown represents the present value of the stock options at the date of grant as determined using the Black-Scholes pricing model. In calculating the present value of the stock options granted, the following assumptions were utilized in May and December 2005: (i) the

continuously compounded risk-free rate of return expressed on a weighted average annual basis was 3.9% and 4.1%, respectively; (ii) expected volatility of the underlying Common Stock was 23.8% and 21.0%, respectively; (iii) expected lives of the stock options granted were 5 years in both instances; and (iv) dividends on the underlying Common Stock increased at an annual rate of 4.8% in both instances. These assumptions are used

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for estimation purposes only. No assurance can be given that actual experience will correspond to the assumptions utilized.

(4) Mr. Tauber was appointed to the Board on June 21, 2005.

(5) Mr. Hansen was appointed to the Board on October 19, 2005.

**CORPORATE GOVERNANCE**

**General**

The Company adopted Corporate Governance Guidelines in 2004, and the Nominating/ Corporate Governance Committee reviews and assesses the adequacy of those guidelines annually. Based upon its review, the Nominating/ Corporate Governance Committee recommended, and the Board adopted, amendments to the Corporate Governance Guidelines in 2006. You may obtain the Corporate Governance Guidelines and the charters of each of the Board's committees, including the Audit Committee, the Compensation Committee and Nominating/ Corporate Governance Committee, on our website, [www.flagstar.com](http://www.flagstar.com). These documents are also available in print upon written request to Paul Borja, CFO, Flagstar Bancorp, Inc., 5151 Corporate Drive, Troy, Michigan 48098.

**Code of Business Conduct and Ethics**

The Board of Directors has adopted a Code of Business Conduct and Ethics (the Code of Conduct) that applies to actions of the employees, officers and directors of the Company including the principal executive officer, principal financial officer, and principal accounting officer. Among other things, the Code of Conduct requires compliance with laws and regulations, avoidance of conflicts of interest and insider trading, and reporting of illegal or unethical behavior. Further, the Code of Conduct provides for special ethics obligations for employees with financial reporting obligations. A copy of the Code of Conduct may be found on our website at [www.flagstar.com](http://www.flagstar.com). Also, the Code of Conduct is available in print upon written request to Paul Borja, CFO, Flagstar Bancorp, Inc., 5151 Corporate Drive, Troy, Michigan 48098.

**Stockholder Nominations**

While the Nominating/ Corporate Governance Committee will consider nominees recommended by stockholders, it has not actively solicited recommendations from the Company's stockholders for nominees. Stockholders who wish to nominate candidates for election to the Board at the Annual Meeting must follow the procedures outlined in STOCKHOLDER PROPOSALS.

All stockholder nominations for new directors must be in writing and must set forth as to each director candidate recommended the following: (1) name, age, business address and, if known, residence address of the nominee; (2) the principal occupation or employment of the nominees; (3) the number of shares of Common Stock that are beneficially owned by the nominee; and (4) any other information relating to the person that would be required to be included in a proxy statement prepared in connection with the solicitation of proxies for an election of directors pursuant to applicable law and regulations. Certain information as to the stockholder nominating the nominee for director must be included, such as the name and address of the stockholder and the number of shares of Common Stock which are beneficially owned by the stockholder. The stockholder must promptly provide any other information requested by the Company.

**Independence**

The Board has conducted its annual review of director independence. During this review, the Board considered relationships and transactions during the past three years between each director or any member of his or her immediate family and the Company and its subsidiaries and affiliates, including those reported under CERTAIN TRANSACTION AND BUSINESS RELATIONSHIPS. The purpose of

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the review was to determine whether any such relationship or transactions were inconsistent with a determination that the director is independent.

The Board reviewed and considered two relationships reported under **CERTAIN TRANSACTION AND BUSINESS RELATIONSHIPS**. With respect to Richard S. Elsea, the Board reviewed and considered transactions between John Adams Mortgage Company ( John Adams ), which Richard S. Elsea owns, and the Bank. In 2005, the Bank purchased mortgage loans from John Adams Mortgage Company which resulted in gross income to John Adams Mortgage Company of \$24,899 which is considerably less than 1% of John Adams' gross income. After reviewing and considering the Bank's ongoing business with John Adams, the Board determined that such relationship is not material on the basis that this is routine in nature, was entered into in the ordinary course of business, and was immaterial in amount to both companies. With respect to Michael Lucci, Sr., the Board reviewed and considered that his daughter-in-law, Rebecca Lucci, is employed as an Executive Vice President in the Human Resources department of the Company. After reviewing and considering the relationship, the Board determined that such relationship is not material on the basis that Ms. Lucci is not an executive officer under Rule 16a-1(f) of the Securities Exchange Act of 1934, as amended, because she is not in charge of a principal business unit, division or function and does not perform a significant policy-making function, Ms. Lucci was a Senior Vice President of the Company prior to Mr. Lucci becoming a member of the Board in 2001, Ms. Lucci's employment relationship with the Company is on an arm's length basis, Ms. Lucci is an adult who does not live in the same household as Mr. Lucci, and Mr. Lucci does not have any material interest in the employment relationship between Ms. Lucci and the Company.

Based on the review, the Board has affirmatively determined that directors Charles Bazy, James D. Coleman, Frank D. Angelo, Robert W. DeWitt, Richard S. Elsea, Michael Lucci, Sr., B. Brian Tauber, and Jay J. Hansen are independent in accordance with applicable Securities and Exchange Commission and New York Stock Exchange rules. The Board considered all relevant facts and circumstances in concluding that such persons are independent and have no material relationship with the Company. As of and after the Annual Meeting, a majority of the Board and the entirety of the Board's three standing committees will be independent directors.

### **Director and Executive Officer Stock Ownership Guidelines**

The Board adopted stock ownership requirements for the Company's directors and executive officers. The requirements specify that non-management directors are expected to own or have stock options to purchase at least 1,000 shares of Common Stock. The Board has determined that all of the non-management directors must meet or exceed these requirements prior to July 1, 2006.

Senior officers of the Company are expected to own at least 100 shares, including shares held in a 401(k) Plan.

### **Executive Sessions of Non-Management Directors**

All non-management directors meet in executive session at least four times per year. No employee of the Company may attend or participate in such executive sessions. The Board will annually designate the lead non-management director, or Lead Director, to chair the executive sessions and to establish and distribute an agenda for each such meeting. Charles Bazy has been designated the Lead Director for 2006.

### **Communications with the Board or the Lead Director**

Individuals who have an interest in communicating directly with the Board or the non-management members of the Board may do so by directing the communication to the Board of Directors or Lead Director. The Lead Director is the presiding director for non-management sessions of the Board of Directors. Any communications should be sent to the following address: Flagstar Bancorp, Inc., 5151 Corporate Drive, Troy, Michigan, 48098. Following each meeting of the non-management directors, the Lead Director determines whether any communication necessitates discussion by the full Board.

**Table of Contents****Succession Plan**

Pursuant to the Corporate Governance Guidelines, the Chief Executive Officer and the Nominating/ Corporate Governance Committee review succession planning with the Board on an annual basis. The Board has adopted a succession plan that is consistent with industry practice and would provide for an orderly transition in case of a catastrophic event involving the Chairman or the Chief Executive Officer.

**SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS**

Persons and groups beneficially owning more than 5% of the Common Stock are generally required under federal securities laws to file certain reports with the Securities and Exchange Commission ( SEC ) detailing such ownership. The term beneficial ownership means the shares held as of the Record Date plus shares underlying any options that are exercisable as of or within 60 days before or after the Record Date. The following table sets forth, as of the Record Date, certain information as to the Common Stock beneficially owned by any person or group of persons who are known to the Company to be the beneficial owners of more than 5% of the Common Stock. Other than as disclosed below, management knows of no person who beneficially owned more than 5% of the Common Stock at the Record Date.

Name and Address of Beneficial Owner (a)(b)	Amount and nature of Beneficial Ownership (c)	Percent of Class (d)
Thomas J. Hammond	11,730,138(e)	18.5%
Janet G. Hammond	4,333,106(f)	6.8
Mark T. Hammond	6,362,001(g)	9.9
Carrie C. Langdon	3,593,630(h)	5.7

- (a) The address of record for each of the individuals named below is c/o Flagstar Bancorp, Inc., 5151 Corporate Drive, Troy, Michigan 48098.
- (b) Mr. Thomas Hammond is the husband of Ms. Hammond. Further, Mr. Mark Hammond and Mr. Langdon are the adult children of Mr. Thomas Hammond and Ms. Hammond.
- (c) These amounts include beneficial ownership of shares with respect to which voting or investment power may be deemed to be directly or indirectly controlled, but does not include stock owned by each stockholder's spouse, as to which the respective person disclaims beneficial ownership.
- (d) The percentage owned is calculated for each stockholder by dividing (i) the total number of outstanding shares beneficially owned by such stockholder as of April 12, 2006 (the Record Date) plus the number of shares such person has the right to acquire within 60 days of the Record Date, into (ii) the total number of outstanding shares as of the Record Date plus the total number of shares that such person has the right to acquire within 60 days of the Record Date.
- (e) This amount includes 11,009,440 shares held indirectly in a revocable living trust, 53,128 shares held indirectly in the Flagstar Bank 401(k) Plan, 17,062 shares of restricted stock, and stock options exercisable as of the Record Date, or that will become exercisable within 60 days thereafter, to purchase 650,398 shares of Common Stock.
- (f) These shares are held indirectly in a revocable living trust.
- (g)

This amount includes 5,520,713 shares held indirectly in a revocable living trust, 24,265 shares of restricted stock, and stock options exercisable as of the Record Date, or that will become exercisable within 60 days thereafter, to purchase 817,023 shares of Common Stock.

- (h) This amount includes 3,373,630 shares held indirectly in a revocable living trust and 220,000 shares held indirectly in a limited liability company.

Table of Contents**EXECUTIVE OFFICERS**

The following table sets forth the name and age (as of the Record Date) of the Company's executive officers.

<b>Name and Age</b>	<b>Position(s) Held in 2005</b>
Thomas J. Hammond, 62	Chairman of the Board of the Company and the Bank
Mark T. Hammond, 40	Vice Chairman, President and Chief Executive Officer of the Company and the Bank
Paul D. Borja, 45	Executive Vice-President, Chief Financial Officer and Treasurer of the Company and the Bank
Kirstin Hammond, 40	Executive Director and Chief Investment Officer of the Company and the Bank
Robert O. Rondeau, Jr., 40	Executive Director of the Company and the Bank

**Thomas J. Hammond** has served as Chairman of the Board of Directors of the Company since 1993, and served as President from 1993 through 1995 and Chief Executive Officer from 1993 through 2002. Mr. Hammond founded the Bank in 1987 and he has served as Chairman of the Board of Directors of the Bank since that time. Mr. Hammond is the father of Mark T. Hammond, President, Chief Executive Officer and Vice Chairman of the Board of Directors, and is the father-in-law of Kirstin A. Hammond and Robert O. Rondeau, Jr., each of whom is an Executive Director of the Company and the Bank and a member of the Board of Directors of the Company.

**Mark T. Hammond** has served as Vice Chairman of the Board of Directors of the Company and of the Bank since 1993, as President of the Company and the Bank since 1995, and as Chief Executive Officer of the Company and the Bank since 2002. Prior to being named President, Mr. Hammond was a Senior Vice President responsible for sales and secondary marketing and served in various other positions in the Bank since 1987. Mr. Hammond is a graduate of the Wharton School of Business (University of Pennsylvania), where he received a Bachelor's Degree in 1987, and has served on the President's Advisory Board of Fannie Mae. Mr. Hammond is the son of Thomas J. Hammond, the husband of Kirstin A. Hammond, and the brother-in-law of Robert O. Rondeau, Jr.

**Paul D. Borja** has served as Executive Vice-President of the Company and the Bank since May 25, 2005, and also as its Chief Financial Officer since June 20, 2005. Previously, he was a partner with the law firm Kutak Rock LLP since 1997 with a practice involving federal tax, banking, corporate law and federal securities law matters and with other law firms since 1990. Prior to practicing law, Mr. Borja was a CPA with Peat Marwick Mitchell, a predecessor to KPMG, from 1982 through 1987, primarily as an auditor of banks and savings and loans. Mr. Borja received his master's degree in tax law from Georgetown University in 1991, his law degree from George Washington University in 1990, and his bachelor's degree in accounting from the University of Notre Dame in 1982.

**Kirstin A. Hammond** has served as a Member of the Board of Directors of the Company since 2002. She also serves as an Executive Director of the Company and the Bank where she has been employed since 1991. Prior to joining the Bank, Ms. Hammond worked as an Investment Analyst at Manufacturer's National Bank from 1987 to 1991. Ms. Hammond graduated from the University of Michigan with a Masters degree in Business Administration in 1991 and from the Wharton School of Business (University of Pennsylvania) with a Bachelor's Degree in 1987. Ms. Hammond is the wife of Mark T. Hammond, the daughter-in-law of Thomas J. Hammond, and the sister-in-law of Robert O. Rondeau, Jr.

**Robert O. Rondeau, Jr.** has served as a Member of the Board of Directors of the Company since 2002. He also serves as an Executive Director of the Company and the Bank, where he has been employed since 1995. Prior to joining the Bank, Mr. Rondeau received a Masters degree in Business Administration from Michigan State University in 1996 and a Bachelor's Degree from Northwestern University in 1987. Mr. Rondeau is the son-in-law of Thomas J. Hammond and the brother-in-law of Mark T. Hammond and Kirstin A. Hammond.

**Table of Contents****SECURITY OWNERSHIP OF MANAGEMENT**

The following table sets forth, as of the Record Date, certain information known to the Company as to the Common Stock beneficially owned by each director, each named executive officer listed in EXECUTIVE COMPENSATION Summary Compensation Table, and all directors and executive officers of the Company as a group. A total of 63,488,777 shares of Common Stock were issued and outstanding as of the Record Date.

Name of Beneficial Owner	Amount and Nature of Beneficial Ownership (a)(b)	Percent of Class
Thomas J. Hammond	11,730,138(c)	18.3%
Mark T. Hammond	6,362,001(d)	9.9%
Charles Bazy	58,542	*
James D. Coleman	29,665	*
Richard S. Elsea	27,825(e)	*
Kirstin A. Hammond	144,270(f)	*
Michael Lucci, Sr.	12,500(g)	*
Frank D. Angelo	2,800	*
Robert Dewitt	3,850(h)	*
Robert O. Rondeau, Jr.	212,182(i)	*
B. Brian Tauber	2,500(j)	*
Jay J. Hansen	0	*
Paul D. Borja	26,903(k)	*
All directors and executive officers as a group	18,612,876	29.6%

\* Less than 1.0%

- (a) These amounts include beneficial ownership of shares with respect to which voting or investment power may be deemed to be directly or indirectly controlled, but does not include stock owned by each stockholder's spouse, as to which the respective person disclaims beneficial ownership.
- (b) These amounts set forth below include options exercisable as of the Record Date, or that will become exercisable within 60 days thereafter, to purchase shares of Common Stock for the following persons: Mr. Thomas Hammond, 650,398 shares, Mr. Mark Hammond, 817,023 shares, Mr. Bazy, 5,875 shares, Mr. Coleman, 15,250 shares, Mr. Elsea, 2,500 shares, Ms. Hammond, 86,613 shares, Mr. Lucci, 2,500 shares, Mr. D. Angelo, 2,500 shares, Mr. Dewitt, 2,500 shares, Mr. Rondeau, 77,273 shares, Mr. Borja, 11,429 shares, and all directors and executive officers as a group, 1,673,861 shares.
- (c) This amount includes 11,009,440 shares held indirectly in a revocable living trust, 17,062 shares of restricted stock and 53,128 shares held indirectly in the Flagstar Bank 401(k) Plan.
- (d) This amount includes 5,520,713 shares held indirectly in a revocable living trust and 24,265 shares of restricted stock.
- (e) This amount includes 10,925 shares held indirectly in a marital trust and 14,400 shares held indirectly in a deferred compensation trust.



- (f) This amount includes 51,042 shares held indirectly in a revocable living trust, 2,275 shares of restricted stock and 4,340 shares held indirectly in the Flagstar Bank 401(k) Plan.
- (g) This amount includes 10,000 shares held indirectly in a revocable living trust.
- (h) This amount includes 1,350 shares held indirectly by Mr. DeWitt's wife.

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- (i) This amount includes 104,867 shares held indirectly in a revocable living trust, 2,275 shares of restricted stock and 27,767 shares held indirectly in the Flagstar Bank 401(k) Plan. This amount does not include 2,890,430 shares held by his wife as to which he disclaims beneficial ownership.
- (j) This amount includes 2,500 shares held indirectly in a revocable living trust.
- (k) This amount includes 4,028 shares of restricted stock.

**EXECUTIVE COMPENSATION**

The following tables set forth information with respect to the compensation paid or accrued by the Company and its subsidiaries during the fiscal years ended December 31, 2005, 2004 and 2003, to or on behalf of its Chief Executive Officer and each of the four most highly compensated executive officers other than the Chief Executive Officer who were serving as of December 31, 2005 ( Named Executive Officers ), in all capacities in which they served:

**Summary Compensation Table**

Name and Principal Position(s)	Year	Salary	Bonus (1)	Other Annual Restricted CompensationStock		Long-Term Compensation Awards		All Other Compensation (5)(6)	Total Compensation (7)
				(2)	Awards(3)	Securities Underlying Option/SARs (4) (#)	(\$)		
Thomas J. Hammond Chairman of the Board	2005	\$ 562,500	\$ 756,000	\$	\$ 252,000	120,000	\$ 252,000	\$ 6,300	\$ 1,828,800
	2004	750,000	1,332,000		1,165,000	100,452	832,500	6,150	4,085,650
	2003	405,308	2,000,000		1,415,315			6,000	3,826,623
Mark T. Hammond Vice Chairman, President and Chief Executive Officer	2005	\$ 756,756	\$ 1,075,200	\$	\$ 358,400	170,667	\$ 358,400	\$ 6,300	\$ 2,555,056
	2004	756,756	1,776,000		888,000	133,937	888,000	6,150	4,314,906
	2003	720,720	2,500,000		799,590	145,144	870,861	6,000	4,897,171
Paul D. Borja(8) Executive Vice President, Chief Financial Officer and Treasurer	2005	\$ 235,680	\$ 151,200	\$	\$ 90,416	35,429	\$ 90,416	\$ 162,065	\$ 729,777
	2004								
	2003								

Kirstin A. Hammond	2005	\$ 333,801	\$ 100,800	\$ 33,600	16,000	\$ 33,600	\$ 6,300	\$ 508,101
Executive Director	2004	333,801	166,500	83,250	12,557	83,250	6,150	672,951
	2003	292,995	250,000	52,740	18,210	109,260	6,000	710,995
Robert O. Rondeau, Jr.	2005	\$ 308,296	\$ 100,800	\$ 33,600	16,000	\$ 33,600	\$ 6,300	\$ 482,596
Executive Director	2004	308,296	166,500	83,250	12,557	83,250	6,150	647,446
	2003	273,316	250,000	52,740	18,210	109,260	6,000	691,316

- (1) The Named Executive Officers received a portion of their annual bonus for the year ended December 31, 2005 in the form of restricted stock and will receive the remainder in the form of stock appreciation rights if PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is approved by stockholders. If PROPOSAL V is not approved, the Compensation Committee intends to grant stock options in lieu of stock appreciation rights. For the years ended December 31, 2004 and 2003, the Named Executive Officers received portions of their annual bonus in the form of restricted stock and stock options. The value of the restricted stock and the number of stock appreciation rights/stock options delivered as part of the annual bonus are reported in Restricted Stock Awards and Securities Underlying Option/ SARs columns of this table.
- (2) In accordance with applicable SEC rules, this column excludes perquisites and other personal benefits if such amounts, in the aggregate, do not exceed \$50,000 or 10% of annual salary and bonus for either year.
- (3) This amount reflects the grant date value of shares of restricted stock granted by the Company to the Named Executive Officers as part of their annual bonus for 2005. The number of shares of restricted stock granted to the Named Executive Officers was as follows: 17,062 for Mr. Thomas Hammond; 24,265 for Mr. Mark Hammond; 3,412 for Mr. Borja; 2,275 for Ms. Hammond; and

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2,275 for Mr. Rondeau. The shares of restricted stock granted as part of the annual bonus for 2005 vests in two equal annual installments, one and two years from the date of grant.

In addition, the amount for Mr. Borja reflects the grant date value of 2,068 shares of restricted stock that he received as part of his signing bonus in accordance with the terms of his employment agreement. The restricted stock granted as part of his signing bonus vests in two equal installments, six-months and one year from the date of grant.

As of December 31, 2005, the number and value (based upon the closing price of the Common Stock on December 20, 2005) of the Named Executive Officers' restricted stock holdings were as follows: 28,545 (\$411,048) for Mr. Thomas Hammond; 21,423 (\$308,491) for Mr. Mark Hammond; 1,034 (\$14,890) for Mr. Borja; 2,008 (\$28,915) for Ms. Hammond; and 2,008 (\$28,915) for Mr. Rondeau. These amounts do not reflect shares of restricted stock granted as part of the Named Executive Officer's annual bonus for 2005.

The Named Executive Officers do not receive dividends on shares of restricted stock prior to vesting and, after vesting, they receive dividends at the same rate and frequency as all stockholders of the Company.

- (4) The dollar amount reflects the portion of the Named Executive Officer's annual bonus for 2005 that will be paid in the form of stock appreciation rights if PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is approved by stockholders. If PROPOSAL V is not approved, the Compensation Committee intends to grant stock options in lieu of stock appreciation rights.

The number of stock appreciation rights granted to each Named Executive Officer is for illustrative purposes only. The number of stock appreciation rights was calculated based upon the present value of the stock appreciation rights granted utilizing the Black-Scholes pricing model with the following assumptions: (i) the continuously compounded risk-free rate of return expressed on a weighted average annual basis was 4.32%, (ii) expected volatility of the underlying Common Stock was 21.2%, (iii) expected lives of the stock appreciation rights granted were 5 years; and (iv) dividends on the underlying Common Stock increased at an annual rate of 4.0%. No assurance can be given that actual experience will correspond to the assumptions utilized. The actual number of stock appreciation rights will be calculated using the Black-Scholes pricing model at the date of grant. In addition, Mr. Borja was granted 11,439 stock options as part of his signing bonus, and these stock options are also reflected in this amount. The value of the stock options granted to Mr. Borja represents the present value of the stock options at the date of grant as determined using the Black-Scholes pricing model and explained in footnote 2 to the Option/ SAR Grants In Last Fiscal Year table below.

The Named Executive Officers received stock options in 2004 and 2003.

- (5) These amounts include Company matching contributions under the Flagstar Bank 401(k) Plan during 2005 of \$6,300 for each Named Executive Officer, other than Mr. Borja. For Mr. Borja, this amount includes Company matching contributions under the Flagstar Bank 401(k) Plan of \$4,575 and a signing bonus and relocation expenses of \$157,490.
- (6) In 2003, the Company discontinued its split dollar life insurance benefit for its executives. In dissolving the program, the individual executive was issued the policy and the Company's basis in the policy was included in the distribution. The Company distributed to Mr. Thomas Hammond, Mr. Mark Hammond, Ms. Hammond, and Mr. Rondeau totaled \$1,114,791, \$477,272, \$171,532, and \$137,224, respectively.
- (7) Consists of a sum of the compensation amounts that are reflected in this table.
- (8) Mr. Borja commenced working for the Company in May 2005, and the salary and bonus amounts are for May through December 2005.

**Table of Contents****Option/ SAR Grants In Last Fiscal Year**

The following table contains information concerning the grant, with respect to Paul D. Borja, of stock options under the 1997 Employees and Directors Stock Option Plan and, with respect to each of the Named Executive Officers, of stock appreciation rights under the 2006 Equity Incentive Plan if PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is approved by stockholders. If PROPOSAL V is not approved, the Compensation Committee intends to instead provide the Named Executive Officers with a grant of stock options under the 1997 Employees and Directors Stock Options Plan as compensation for their annual bonus earned during 2005.

**Individual Grants**

	Number of Securities Underlying Options/SARs Granted	Percent of Total Options/SARs Granted to Employees in Fiscal Year	Exercise Price (\$ per share) (1)	Expiration Date	Grant Date Present Value (2)
Thomas J. Hammond	120,000(3)	25.6%	\$ 14.77	1/24/13	\$ 252,000
Mark T. Hammond	170,667(3)	36.5	14.77	1/24/13	358,400
Paul D. Borja	24,000(3)	5.1	14.77	1/24/13	50,400
	11,429(4)	3.1	19.35	2/25/15	40,016
Kirstin A. Hammond	16,000(3)	3.4	14.77	1/24/13	33,600
Robert O. Rondeau, Jr.	16,000(3)	3.4	14.77	1/24/13	33,600

- (1) The exercise price of the stock options granted to Mr. Borja were calculated using the average of the high and the low stock price on the date of grant. The exercise price of the stock appreciation rights will be the average of the high and low stock price on the date of grant. The exercise price shown is for illustrative purposes only and is based on the average of the high and low stock price on February 3, 2006.
- (2) For the stock options granted to Mr. Borja, this amount represents the present value of the stock options at the date of grant as determined using the Black-Scholes pricing model. In calculating the present value of the stock options granted, the following assumptions were utilized: (i) the continuously compounded risk-free rate of return expressed on a weighted average annual basis was 3.8%, (ii) expected volatility of the underlying Common Stock was 28.3%, (iii) expected lives of the stock options granted were 5 years; and (iv) dividends on the underlying Common Stock increased at an annual rate of 4.8%. These assumptions are used for illustrative purposes only. No assurance can be given that actual experience will correspond to the assumptions utilized. For the stock appreciation rights that will be granted to the Named Executive Officers if stockholders approve PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN, this amount represents the value of the stock appreciation rights at the date of grant that has been approved by the Compensation Committee as compensation for the annual bonus earned during 2005. On the date of grant, the number of stock appreciation rights will be calculated using the Black-Scholes pricing model.
- (3) If PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is approved by stockholders, the stock appreciation rights granted under the 2006 Equity Incentive Plan would vest annually over a period of four years with the first vesting occurring on February 3, 2007 and an equal amount vesting on February 3, 2008, 2009 and 2010. The number of stock appreciation rights granted is for illustrative purposes only. The calculation of the number of stock appreciation rights is explained in footnote 5 to the Summary Compensation Table

above. If PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is not approved, the Compensation Committee intends to instead provide the Named Executive Officers with a grant of stock options

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under the 1997 Employees and Directors Stock Options Plan as compensation for their annual bonus earned during 2005.

- (4) These stock options granted under the 1997 Employees and Directors Stock Option Plan have vested.

**Aggregate Option/SAR Exercises in Last Fiscal Year and Fiscal Year End Option/SAR Values**

The following table sets forth information concerning (i) the amount of stock options exercised by the Named Executive Officers during fiscal year 2005 and (ii) the number and value of unexercised stock options and stock appreciation rights that were held by the Named Executive Officers at December 31, 2005. The stock appreciation rights will only be granted under the 2006 Equity Incentive Plan if PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is approved by stockholders. If PROPOSAL V is not adopted, the Compensation Committee intends to instead provide the Named Executive Officers with a grant of stock options under the 1997 Employees and Directors Stock Options Plan as compensation for their annual bonus earned during 2005.

Name	Shares Acquired On Exercise	Value Realized (1)	Number of Securities Underlying Unexercised Options/SARs at Fiscal Year End (2)		Value of Unexercised In-The-Money Options/SARs at Fiscal Year End (2)(3)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Thomas J. Hammond	562,500	\$ 9,969,075	848,398	120,000	\$ 3,171,605	\$ 0
Mark T. Hammond	800,000	8,825,862	744,451	410,811	1,380,929	556,157
Paul D. Borja			11,429	24,000	0	0
Kirstin A. Hammond			77,509	44,210	189,358	64,787
Robert O. Rondeau, Jr.	23,283	251,718	68,169	44,210	88,687	64,787

- (1) Represents the amount equal to the excess of the fair value of the shares at the time of exercise over the exercise price of the stock options.
- (2) The number of stock appreciation rights granted is for illustrative purposes only and is included in the unexercisable column. The calculation of the number of stock appreciation is explained in footnote 5 to the Summary Compensation Table above. If PROPOSAL V ADOPTION OF THE 2006 EQUITY INCENTIVE PLAN is not approved, the Compensation Committee intends to instead provide the Named Executive Officers with a grant of stock options under the 1997 Employees and Directors Stock Options Plan as compensation for their annual bonus earned during 2005.
- (3) Represents the difference between the closing price of the common stock on December 30, 2005 (\$14.40 per share) and the exercise price of the stock options and stock appreciation rights.

**Employment Agreements**

The Company has entered into employment agreements with each of the Named Executive Officers. The Named Executive Officers are responsible for overseeing all operations of the Company and for implementing the policies adopted by the Board. The Board believes that the agreements assure fair treatment of these Executive Officers in relation to their career, providing them with a limited form of financial security while committing them to future employment for the term of their respective agreements. In the event that an Executive Officer with an employment agreement prevails over the Company in a legal dispute regarding such person's employment agreement, he or she will be reimbursed for his or her legal and other expenses.

The term of each agreement is three years, and each agreement provides for an annual base salary. On each anniversary date from the date of commencement of the agreements, the term of the Named Executive Officer's employment under the agreements will be extended for an additional one-year period



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beyond the then effective expiration date, upon a determination by the Board that the performance of the Named Executive Officer has met the required performance standards and that such agreements should be extended. The agreements provide the Named Executive Officers with a salary review by the Board not less often than annually, as well as with inclusion in any discretionary bonus plans, retirement and medical plans, customary fringe benefits, vacation, and sick leave.

The agreements terminate upon the Executive Officer's death or disability, and are terminable by the Company for just cause as defined in the agreements. In the event of termination for just cause, no severance benefits are available. If the Company terminates the Executive Officer, other than Mr. Borja, without just cause, such Executive Officers will be entitled to a continuation of his or her salary and benefits from the date of termination through the remaining term of such Executive Officer's agreement, plus an additional 12-month period, and, at such Executive Officer's election, either cash in an amount equal to the cost to such Executive Officer of obtaining health, life, disability, and other benefits which such Executive Officer would have been eligible to participate in through the agreement's expiration date or continued participation in such benefit plans through the agreement's expiration date, provided such Executive Officer continued to qualify for participation therein. Mr. Borja would be entitled to continuation of his salary and benefits for 12 months from the date of termination without just cause. If the agreements are terminated due to the Executive Officer's disability (as defined in the agreements), the Executive Officer will be entitled to a continuation of his or her salary and benefits for up to 180 days following such termination. In the event of the Executive Officer's death during the term of the agreement, his or her estate will be entitled to receive his or her salary through the last day of the calendar month in which the Executive Officer's death occurred. The Executive Officer is able to terminate voluntarily his or her agreement by providing 90 days' written notice to the Board, in which case the Executive Officer is entitled to receive only his or her compensation, vested rights and benefits up to the date of termination.

The agreements contain provisions stating that in the event of the Executive Officer's involuntary termination of employment in connection with, or within one year after, any change in control of the Company, other than for just cause, the Employee will be paid within 10 days of such termination an amount equal to the difference between (i) 2.99 times his or her base amount, as defined in Section 280G(b)(3) of the Code, and (ii) the sum of any other parachute payments, as defined under Section 280G(b)(2) of the Code, that the Employee receives on account of the change in control. Control generally refers to the acquisition, by any person or entity, of the ownership or power to vote more than 50% of the Company's voting stock, the control of the election of a majority of the Company's directors, or the exercise of a controlling influence over the management or policies of the Company. In addition, under the agreements, a change in control occurs when, during any consecutive two-year period, directors of the Company at the beginning of such period cease to constitute at least a majority of the Board. The amount determined using the foregoing formula would also be paid (a) in the event of an Executive Officer's involuntary termination of employment within 30 days following a change in control, or (b) in the event of the Executive Officer's voluntary termination of employment within one year following a change in control, upon the occurrence, or within 90 days thereafter, of certain specified events following the change in control, which have not been consented to in writing by the Employee, including (i) the requirement that the Employee perform his or her principal executive functions more than 50 miles from his or her primary office, (ii) a reduction in the Executive Officer's base compensation as then in effect, (iii) the failure of the Company to continue to provide the Employee with contractual compensation and benefits, including material vacation, fringe benefits, stock option and retirement plans, (iv) the assignment to the Employee of duties and responsibilities which are other than those normally associated with his or her position with the Company, (v) a material reduction in the Executive Officer's authority and responsibility, and (vi) in the case of an employee who is also a director, the failure to re-elect the Executive Officer to the Board. The aggregate payments that would be made to these Executive Officers assuming termination of employment, other than for just cause, within one year of the change in control at January 1, 2006, would be approximately as follows: Thomas J. Hammond \$21.9 million; Mark T. Hammond - \$23.0 million; Paul D. Borja \$1.6 million; Kirstin A. Hammond \$2.1 million; Robert O. Rondeau, Jr. \$2.0 million.



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**Employee Stock Acquisition Plan**

The Company terminated the 1997 Employee Stock Acquisition Plan ( Purchase Plan ) in November 2005. The purpose of the Purchase Plan was to encourage broad-based ownership by employees of the Company and, as a result, to provide an incentive for employees at all levels to contribute to the profitability and success of the Company. Costs incurred by the Company pursuant to the Purchase Plan were deductible as an expense by the Company. During 2005, the Company paid out \$82,000 pursuant to this plan.

**1997 Incentive Compensation Plan**

The Company has also implemented the 1997 Incentive Compensation Plan (the Incentive Compensation Plan ). Benefits under the Incentive Compensation Plan are payable only in the form of cash from the Company's general assets. The purposes of the Incentive Compensation Plan is to attract and retain the best available personnel for positions of substantial responsibility with the Company and to provide additional incentives to employees of the Company in the event the Company achieves certain financial performance goals. If PROPOSAL V ADOPTION OF 2006 EQUITY INCENTIVE PLAN is approved by stockholders, then the Incentive Compensation Plan will be consolidated in the 2006 Equity Compensation Plan.

The Incentive Compensation Plan is administered by the Compensation Committee. The Compensation Committee decides, from year to year, which employees of the Company are eligible to participate in the Incentive Compensation Plan and the size of the bonus pool. Directors who are not employees may not participate in the Incentive Compensation Plan.

Each employee who is eligible to receive a bonus at the end of a plan year will receive a bonus equal to a predetermined amount adjusted by a mathematical formula that reflects aspects of the Company's results for that year. The aggregate amount of bonuses payable for any plan year will be proportionately reduced to the extent that the payment would cause the Bank to cease to be a well-capitalized institution. For 2005, the Incentive Compensation Plan utilized the results from return on average equity, net interest margin, loan production, asset growth, retail deposit growth, gain on loan sale spread, and efficiency ratio to calculate the incentive payments. The Compensation Committee certified that 56% of the financial performance goals were met in 2005. For 2006, the same criteria will be used although the specific targets have been modified.

**1997 Employees and Directors Stock Option Plan**

The Company adopted the 1997 Employees and Directors Stock Option Plan, as amended (the Stock Option Plan ), to provide a method for compensating its key employees with equity-based performance incentives. The aggregate number of shares of Common Stock reserved for issuance under the Stock Option Plan is 13,727,250 shares, of which there are 1,409,202 available for issuance. If PROPOSAL V ADOPTION OF 2006 EQUITY INCENTIVE PLAN is approved by stockholders, then the Stock Option Plan will be consolidated into the 2006 Equity Compensation Plan.

The Compensation Committee administers the Stock Option Plan and has the discretion to grant options to all employees and directors and those of our affiliates. Subject to the terms of the Stock Option Plan, the Compensation Committee determines the awards to be made under the plan, including incentive stock options and non-incentive stock options, the terms and conditions for each award and the form of agreement to be used.

**2000 Stock Incentive Plan**

The Company adopted the 2000 Stock Incentive Plan, as amended (the Restricted Stock Plan ), to provide an additional incentive to directors, officers, and employees by facilitating their acquisition of common stock. The aggregate number of shares of Common Stock reserved for issuance under the Restricted Stock Plan is 2,750,000 shares, of which there are 859,078 available for issuance. If

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PROPOSAL V ADOPTION OF 2006 EQUITY INCENTIVE PLAN is approved by stockholders, then the Restricted Stock Plan will be consolidated into the 2006 Equity Compensation Plan.

The Compensation Committee administers the Restricted Stock Plan and has the discretion to grant restricted stock, which is stock that is subject to a vesting schedule, or deferred shares, which is stock that immediately vests but is treated as deferred compensation, to directors, officers, and employees. Subject to the terms of the Restricted Stock Plan, the Compensation Committee has sole and complete authority and discretion to select participants and grant awards, determine the form and content of awards to be issued, interpret the Restricted Stock Plan, prescribe, amend and rescind rules and regulations relating to the Restricted Stock Plan, and make other determinations necessary or advisable for the administration of the Restricted Stock Plan.

**REPORT OF THE COMPENSATION COMMITTEE**

**Overview and Philosophy**

The Company's executive officers are also executive officers of the Bank and are compensated by the Bank not the Company. However, the responsibility for setting policies that govern executive compensation, and for recommending the components and structure of the compensation plans for executive officers of the Company rests with the Company's Compensation Committee (the Committee). During 2005, the Committee was comprised of Directors James D. Coleman, Frank D. Angelo and Robert W. DeWitt.

Under the direction of the Committee, the Company has developed and implemented compensation policies and plans that embody a pay-for-performance philosophy. The policies and plans encourage achievement of objectives as formulated by the Company's Board of Directors and its committees and reward exceptional performance as determined by the Committee. In the opinion of the Committee, this approach strengthens the Company's long-term performance by making the goals and objectives of executive management congruent with those of the Company and its stockholders. The Committee also believes that competitive executive compensation and the structure of the Company's compensation plans are essential to the Company's desire to attract and retain qualified management. For 2005, the Committee considered and determined the compensation for each of the executive officers named in the

Summary Compensation Table herein. In 2003, 2004, and 2005, the Committee utilized the services of Clark Consulting as an outside consultant in determining appropriate compensation levels for the executive officers.

**Executive Compensation Programs**

Within overall purpose set forth above in consultation with Clark Consulting, the Committee has determined that the Company's executive compensation program should have the following primary components: base salary; cash bonuses; long-term incentive compensation in the form of stock appreciation rights and restricted stock; and other competitive benefits. The cash bonuses and restricted stock awards for 2005 were issued under the 1997 Incentive Compensation Plan and the 2000 Stock Incentive Plan, respectively. Subject to stockholder approval, the stock appreciation rights for 2005 will be issued under the 2006 Equity Incentive Plan. See PROPOSAL V ADOPTION OF 2006 EQUITY INCENTIVE PLAN below. If PROPOSAL V is not approved by stockholders, the Compensation Committee intends to replace the stock appreciation rights with stock option awards under the 1997 Employee and Directors Stock Option Plan.

Base and incentive compensation for executive officers depends primarily on regional and national surveys of compensation paid to executive officers of other savings and loan holding companies, commercial banks and mortgage lending institutions similar in size, market capitalization, scope of operations and other characteristics, as well as the Company's operating results.

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*Base Compensation.* The Committee has determined that the base compensation for the Company's executive officers should be based primarily on the salaries paid to executives having comparable responsibilities at other similar institutions. A primary, but not the sole, source of information upon which the base compensation of executive officers is based are surveys of compensation paid to executives performing similar functions at other financial institutions and/or mortgage banking companies provided by Clark Consulting. In setting base salaries, the Committee also considers other qualitative factors such as the overall performance of the Company and the personal performance and effectiveness of each officer.

*Incentive Compensation.* The Company has adopted the Incentive Compensation Plan, which relies on the specific performance of the Company each year compared with certain benchmark performance levels. These same goals are used for determining long-term incentive compensation awards. For 2005, the performance goals entailed certain achievements required in the areas of returns on average equity, net interest margin, loan production, asset growth, retail deposit growth, gain on loan sale spread, and our efficiency ratio. Incentive compensation under the Incentive Compensation Plan is issued in the form of cash, the amount of which is generally based upon a mathematical formula. In 2005, the Company met 56% of the financial performance goals set by the Compensation Committee.

*Long-Term Incentive Compensation.* The Compensation Committee believes that the grant of equity-based compensation encourages the Company's executives to focus on managing the Company from the perspective of an equity owner. The Company previously adopted two plans that enable employees and officers to develop an equity interest in Flagstar, the 1997 Employees and Directors Stock Option Plan and the 2000 Stock Incentive Plan. The Company has adopted the 2006 Equity Incentive Plan, subject to shareholder approval, which will consolidate/merge, amend and restate of the 1997 Employees and Directors Stock Option Plan, 2000 Stock Incentive Plan and 1997 Incentive Compensation Plan (the "Incentive Compensation Plan"). See PROPOSAL V ADOPTION OF 2006 EQUITY INCENTIVE PLAN below. The 2006 Equity Incentive Plan would expand the types of equity compensation awards available to the Compensation Committee to include stock appreciation rights, restricted stock units, performance units, performance shares and other awards based on, payable in or otherwise referenced to our common stock. These expanded awards are available in addition to existing awards under our plans, including incentive stock options, nonqualified stock options, restricted stock and performance-based cash payments.

*Other Benefits.* In addition to the foregoing, the Company provides medical, dental and life insurance, a defined contribution pension plan qualifying under Sections 401(a) and Section 401(k) of the Internal Revenue Code of 1986, as amended, to senior executives that are generally available to all Company employees, and other perquisites that are comparable to standards within the financial institutions industry.

### **Compensation of the Chief Executive Officer**

Compensation for Flagstar's Chief Executive Officer, Mark T. Hammond is reviewed annually by the Compensation Committee in consultation with Clark Consulting. Mr. Hammond's compensation for 2005 was determined based on the same general policies and criteria as the compensation for other executive officers. In making its determination of Mr. Hammond's base salary and target bonus for 2005, the Compensation Committee reviewed market survey data provided by Clark Consulting and considered the financial and operating results of Flagstar relative to its peer group. The percentage of target bonus awarded to Mr. Hammond in the form of incentive compensation and long-term incentive compensation was calculated based upon the same formula and in the same manner as described above for the other executive officers and was based on the Company's achievement of predetermined goals in the following areas: returns on average equity, net interest margin, loan production, asset growth, deposit growth, gain on loan sale spread and efficiency ratio. For 2005, the Compensation Committee determined that the Company met 56% of the financial performance goals that had been set for the above-referenced areas. Therefore, Mr. Hammond was awarded a cash bonus of \$1,075,200, 170,667 stock appreciation rights that may only be settled in cash, and 24,265 shares of restricted stock.

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The Committee believes that Mr. Hammond's total compensation for 2005 appropriately reflected his contribution to the Company's financial results.

**COMPENSATION COMMITTEE**

James D. Coleman,  
Chairman  
Frank D. Angelo  
Robert W. DeWitt

**Compensation Committee Interlocks and Insider Participation**

None of the members of the Compensation Committee has at any time been an officer or employee of the Company or its subsidiaries. Members of the Compensation Committee may, from time to time, have banking relationships in the ordinary course of business with the Bank, as described in the section entitled "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS." No member of the Compensation Committee had any other relationship with the Company during 2005 requiring disclosure as a related party transaction. During 2005, none of our executive officers served as a member of another entity's compensation committee, one of whose executive officers served on our Compensation Committee or was a director of the Company, and none of our executive officers served as a director of another entity, one of whose executive officers served on our Compensation Committee.

**CERTAIN TRANSACTIONS AND BUSINESS RELATIONSHIPS**

The Company and its subsidiaries have had, and expect to have in the future, transactions in the ordinary course of business with directors and executive officers and members of their immediate families, as well as with principal stockholders. The following business transactions were conducted in the ordinary course of business on substantially the same terms as those prevailing for comparable transactions with non-affiliated persons. It is the belief of management that such loans or transactions neither involved more than the normal risk of collection nor presented other unfavorable features.

Michael Lucci, Sr. is a member of the Board, and his daughter-in-law, Rebecca Lucci, is an Executive Vice President in the Human Resources department of the Company. Ms. Lucci's total compensation was \$220,924 in 2005.

Richard Elsea is a member of the Board and the Audit Committee. He is the owner of John Adams Mortgage Company (John Adams), a mortgage origination firm that sells mortgage loans to the Company. John Adams sold \$2.6 million in mortgage loans to the Company during 2005. These sales resulted in gross income to John Adams of only \$24,899 which was considerably less than 1% of its gross income for the year and significantly less than the threshold for reporting related party transactions.

Robert O. Rondeau, Jr. is a Director and an Executive Director of the Company. The Company engaged in certain transaction with Select Financial, a Rhode Island mortgage company owned by Robert and Marie Rondeau, the parents of Mr. Rondeau. Select Financial is a correspondent of the Company and sold \$34.8 million in mortgage loans to the Company during 2005. Select Financial is also a customer that utilizes the Company's warehouse lending program offered through the Company's commercial loan division. Select Financial has an approved line of credit of \$10.3 million at December 31, 2005. The average amount outstanding during 2005 was \$1.3 million, with a high balance of \$4.1 million and a balance at December 31, 2005, of \$0.2 million. During 2005, Select Financial utilized this line 422 times. Robert and Marie Rondeau have personally guaranteed this line of credit.

In addition to the transactions listed above, certain directors and executive officers of the Company and its subsidiaries, and members of their immediate families, were indebted to the Bank as customers in

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connection with mortgage loans and other extensions of credit by the Bank. These transactions were in the ordinary course of business and were on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons. None of these loans have involved more than the normal risk of collectibility or presented other unfavorable features.

**SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's officers and directors, and persons who own more than 10% of a registered class of the Company's equity securities, to file reports of ownership and changes in ownership with the SEC and to furnish the Company with copies of all such reports. Based solely on its review of copies of such reports received by it, or written representations from certain reporting persons that no annual report of change in beneficial ownership is required, the Company believes that Michael W. Carrie, former Executive Director and Chief Financial Officer of the Company, delinquently reported the exercise of stock options, receipt of the underlying shares, and the subsequent sale of shares on June 20, 2005 in a Form 4 filed on June 27, 2005, Messrs. Thomas J. Hammond, Mark T. Hammond and Robert O. Rondeau, Jr. and Ms. Kirstin A. Hammond delinquently reported the withholding of restricted shares for tax purposes on August 26, 2005 in Form 5s filed on February 14, 2006, and Mr. Borja delinquently reported the withholding of restricted shares for tax purposes on December 28, 2005 in Form 4 filed on February 28, 2006. Other than as disclosed above, the Company believes that all filing requirements applicable to its directors, executive officers and greater than 10% beneficial owners during the year ended December 31, 2005 were timely met.

**Table of Contents****STOCK PERFORMANCE GRAPH**

The graph and table that follow show the cumulative return, assuming reinvestment of dividends, on the Common Stock since December 31, 2000. This return is compared in the table and graph with the cumulative return, assuming reinvestment of dividends, over the same period with the following four indices: (1) the Nasdaq Financial 100 Index; (2) the Nasdaq Bank Index; (3) the S&P Small Cap 600 Index; and (4) the Russell 2000 Index. The graph and table were prepared assuming that \$100 was invested on December 31, 2000 in the Common Stock and in each of the indices. Cumulative total return on the Common Stock or the four indices equals the total increase in value since December 31, 2000. The stockholder returns shown on the performance graph are not necessarily indicative of the future performance of the Common Stock or any particular index.

**Cumulative Total Stockholder Return  
Compared With Performance of Selected Indices  
December 31, 2000 Through December 31, 2005**

	<b>Dec-00</b>	<b>Jun-2001</b>	<b>Dec-2001</b>	<b>Jun-2002</b>	<b>Dec-2002</b>	<b>Jun-2003</b>	<b>Dec-2003</b>	<b>Jun-2004</b>	<b>Dec-2004</b>	<b>Jun-2005</b>	<b>Dec-2005</b>
Nasdaq											
Financial	100	104	106	113	104	115	136	139	157	153	161
Nasdaq Bank	100	110	113	128	121	134	160	163	182	175	179
S&P Small											
Cap 600	100	106	107	107	91	103	126	139	155	158	167
Russell 2000	100	107	103	98	82	96	120	128	142	141	149
Flagstar											
Bancorp	100	84	123	212	200	457	406	385	448	385	301



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