



**Audit • Tax • Advisory**

**Grant Thornton LLP**  
2010 Corporate Ridge, Suite 400  
McLean, VA 22102-7838

T 703.847.7500  
F 703.848.9580  
www.GrantThornton.com

## **Report of Independent Certified Public Accountants**

To the Board of Directors of  
Securities Investor Protection Corporation

We have audited the accompanying statement of financial position of Securities Investor Protection Corporation (the Corporation) as of December 31, 2007 and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America as established by the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Securities Investor Protection Corporation as of December 31, 2007, and the changes in net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

*Grant Thornton LLP*

McLean, VA  
April 2, 2008

# Securities Investor Protection Corporation

## Statement of Financial Position as of December 31, 2007

### ASSETS

Cash	\$	289,799
U.S. Government securities, at fair value and accrued interest receivable of (\$18,753,015); (amortized cost \$1,464,560,833) (Note 6)		1,521,967,640
Advances to trustees for customer protection proceedings in progress, less allowance for possible losses (\$167,929,869) (Note 4)		400,000
Other (Note 5 and Note 8)		1,697,016
		<b>\$1,524,354,455</b>

### LIABILITIES AND NET ASSETS

Accrued benefit costs (Note 8)	\$	5,650,987
Accounts payable and other accrued expenses		683,568
Deferred rent		416,213
Estimated costs to complete customer protection proceedings in progress (Note 4)		12,600,000
		19,350,768
Net assets		1,505,003,687
		<b>\$1,524,354,455</b>

## Statement of Activities for the year ended December 31, 2007

Revenues:		
Interest on U.S. Government securities	\$	67,673,900
Member assessments (Note 3)		852,025
		68,525,925
Expenses:		
Salaries and employee benefits (Note 8)		5,818,841
Legal and accounting fees (Note 4)		126,995
Credit agreement commitment fee (Note 5)		1,698,657
Rent (Note 5)		663,850
Other		2,007,620
		10,315,963
Excess estimated future recoveries over provision for estimated costs to complete customer protection proceedings in progress (Note 4)		(264,688)
		10,051,275
Total net revenues		58,474,650
Realized and unrealized gains on U.S. Government securities (Note 6)		63,088,803
Pension and postretirement benefit changes other than net periodic benefit costs (Note 8)		(1,007,696)
Increase in net assets		120,555,757
Net assets, beginning of year		1,384,447,930
Net assets, end of year		<b>\$1,505,003,687</b>

The accompanying notes are an integral part of these statements.

# Securities Investor Protection Corporation

## Statement of Cash Flows for the year ended December 31, 2007

### Operating activities:

Interest received from U.S. Government securities	\$ 62,874,679
Member assessments received	852,025
Advances paid to trustees	(9,730,786)
Recoveries of advances	6,847,394
Salaries and other operating activities expenses paid	(10,016,193)
Net cash provided by operating activities	50,827,119

### Investing activities:

Proceeds from sales of U.S. Government securities	145,750,398
Purchases of U.S. Government securities	(197,002,066)
Purchases of furniture and equipment	(15,738)
Net cash used in investing activities	(51,267,406)

Decrease in cash	(440,287)
Cash, beginning of year	730,086
Cash, end of year	\$ 289,799

The accompanying notes are an integral part of this statement.

## Notes to Financial Statements

### 1. Organization and general

The Securities Investor Protection Corporation (SIPC) was created by the Securities Investor Protection Act of 1970 (SIPA), which was enacted on December 30, 1970, primarily for the purpose of providing protection to customers of its members. SIPC is a nonprofit membership corporation and shall have succession until dissolved by an Act of Congress. Its members include all persons registered as brokers or dealers under Section 15(b) of the Securities Exchange Act of 1934 except for those persons excluded under SIPA.

SIPC is exempt from income taxes under 15 U.S.C. § 78kkk(e) of SIPA and under § 501(c)(6) of the Internal Revenue Code. Accordingly, no provision for income taxes is required.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### 2. The "SIPC Fund" and SIPC's resources

The "SIPC Fund," as defined by SIPA, consists of cash and U.S. Government securities aggregating \$1,522,257,439.

In the event the SIPC Fund is or may reasonably appear to be insufficient for the purposes of SIPA, the Securities and Exchange Commission is authorized to make loans to SIPC and, in that connection, the Commission is authorized to issue notes or other obligations to the Secretary of the Treasury in an aggregate amount not to exceed \$1 billion. In addition, SIPC maintains \$1 billion revolving lines of credit with a consortium of banks.

### 3. Member assessments

For calendar year 2007 each member's assessment is \$150. Assessments received in advance will be applied to future assessments, or refunded to the member after it fulfills certain requirements.

### 4. Customer protection proceedings

Customer protection proceedings (proceedings) include liquidations conducted by court appointed trustees and direct payment proceedings conducted by SIPC. There are 21 proceedings in progress at December 31, 2007. Customer claims have been satisfied in 18 of these proceedings and in 3 proceedings customer claims and distributions are being processed.

Advances to trustees represent net amounts disbursed and amounts currently payable for proceedings in progress, less an allowance for possible losses.

Estimated costs to complete proceedings are accrued based upon the costs of completed cases of comparable size and complexity and other costs that can be reasonably estimated. Recoveries are estimated based upon the expected disposition of the debtors' estates.

SIPC and Trustees appointed under SIPA are subject to legal claims arising out of the proceedings and there are certain legal claims pending seeking coverage under SIPA. These claims are considered in determining estimated costs to complete proceedings and management believes that any liabilities or settlements arising from these claims will not have a material effect on SIPC's net assets.

SIPC has advanced a net of \$168.4 million for proceedings in progress (including direct payment proceedings of \$102 thousand) to carry out its statutory obligation to satisfy customer claims and to pay administration expenses. Of this amount, \$168 million is not expected to be recovered.

The following table summarizes transactions during the year ended December 31, 2007 that result from these proceedings:

	Customer Protection Proceedings	
	Advances to trustees, less allowance for possible losses	Estimated costs to complete
Balance, beginning of year	\$6,400,000	\$21,300,000
Add:		
Provision for current year recoveries	500,000	—
Provision for estimated future recoveries	300,000	—
Provision for estimated costs to complete proceedings	—	500,000
Less:		
Recoveries	6,800,000	—
Advances to trustees	—	9,200,000
Balance, end of year	\$ 400,000	\$12,600,000

Customer payments and related expenses of direct payment proceedings are recorded as expenses as they are incurred.

Legal and accounting fees include fees and expenses of litigation related to proceedings.

These financial statements do not include accountability for assets and liabilities of members being liquidated by SIPC as Trustee. Such accountability is reflected in reports required to be filed with the courts having jurisdiction.

## 5. Commitments

Future minimum rentals for office space in Washington, D.C., under a ten-year lease expiring August 31, 2015, are as follows: 2008 - \$526,790; 2009 - \$539,911; 2010 - \$553,447; 2011 - \$567,259; 2012 - \$581,485; 2013 - \$595,988; 2014 - \$610,905; 2015 - \$417,490; for a total of \$4,393,275 as of December 31, 2007. Additional rental based on increases in operating expenses and real estate taxes is required by the lease. The rent holiday of \$41,567 and the leasehold improvement incentive of \$345,300 are being amortized over the life of the lease.

On August 31, 2007 SIPC renewed its lease for additional office space in Fairfax, Virginia. The new five-year lease commences on August 1, 2008. Future minimum rentals for the space, expiring on July 31, 2013, are as follows: 2008 - \$98,900; 2009 - \$106,312; 2010 - \$109,502; 2011 - \$112,787; 2012 - \$116,171; 2013 - \$68,937; for a total of \$612,609 as of December 31, 2007. Additional rental is based on increases in operating expenses including real estate taxes as required by the lease.

In March, 2004, SIPC entered into a \$1 billion credit agreement with a consortium of banks, consisting of (i) a \$500 million, 364-day, revolving credit facility, with a commitment fee of .09% per annum, and (ii) a \$500 million, 3-year, revolving credit facility at .11% per annum, both paid quarterly. Additionally, fees ranging from .2% to .3% were paid to certain banks based on the level of their commitment.

In March, 2006, the \$500 million, 364-day, revolving credit facility with a commitment fee of .09% per year was replaced by a new 3-year, \$500 million revolving credit facility with commitment fees of .10% per year. Additionally, upfront fees averaging .14% were paid to certain banks.

In March, 2007, a new \$500 million, 3-year revolving credit facility with a commitment fee of .10% per year was entered into, replacing the expiring March, 2004, 3-year credit agreement. Upfront fees ranging from .12% to .15% were paid to certain banks based on the level of their commitment.

## 6. Fair value of securities

Fair value of U.S. Government securities is based on the Federal Reserve Bank of New York bid quote as of December 31, 2007.

U.S. Government securities as of December 31, 2007, included gross unrealized gains of \$57,424,316 and gross unrealized losses of \$17,509.

## 7. Reconciliation of increase in net assets to net cash provided by operating activities:

Increase in net assets	\$120,555,757
Unrealized gain on U.S. Government securities	(63,088,803)
Net decrease in estimated cost to complete customer protection proceedings	(8,700,000)
Net decrease in estimated recoveries of advances to trustees	6,000,000
Net amortized premium on U.S. Government securities	(4,350,577)
Increase in payables and accrued expenses	480,835
Increase in accrued interest receivable on U.S. Government securities	(448,644)
Decrease in prepaid expenses	212,890
Depreciation and amortization	160,201
Increase in deferred rent	4,802
Loss on disposal of assets	658
Net cash provided by operating activities	\$ 50,827,119

## 8. Pensions and Other Postretirement Benefits

SIPC has a noncontributory defined benefit plan and a contributory defined contribution plan which cover all employees. SIPC also has a supplemental non-qualified retirement plan for certain employees. The \$195,338 year end market value of the supplemental plan is reflected in Other assets and as a deferred compensation liability in Accrued benefit costs. In addition SIPC has two defined benefit post-retirement plans that cover all employees. One plan provides medical and dental insurance benefits and the other provides life insurance benefits. The postretirement health care plan is contributory, with retiree contributions adjusted annually to reflect changes in gross premiums; the life insurance plan is noncontributory.

The provisions of Statement of Financial Accounting Standard No. 158 (FAS 158) (an amendment of FAS 132, 106, and 87) requires SIPC to recognize in the Statement of Financial Position the overfunded or underfunded status of the plans as an asset or liability in the Statement of Financial Position and to recognize the funded status in the year in which the change occurs through the Statement of Activities. In addition, SIPC is required to recognize within the Statement of Activities, gains and losses due to differences between actuarial assumptions and actual experience and any effects on prior service due to plan amendments that arise during the period and which are not being recognized as net periodic benefit costs.

	<b>Pension Benefits</b>	<b>Other Postretirement Benefits</b>
<b>Change in Benefit Obligation</b>		
Benefit obligation at beginning of year	\$19,337,878	\$ 4,752,607
Service cost	658,238	152,966
Interest cost	1,143,346	282,984
Plan participants' contributions	-	11,372
Amendments	184,452	-
Actuarial loss (gain)	648,231	145,911
Benefits paid	(672,511)	(66,682)
<b>Benefit Obligation at end of year</b>	<b>\$21,299,634</b>	<b>\$ 5,279,158</b>
<b>Change in Plan Assets</b>		
Fair value of plan assets at beginning of year	\$19,912,391	\$ -
Actual return on plan assets	1,383,263	-
Employer contributions prior to measurement date	500,000	-
Employer contributions	-	55,310
Plan participants' contributions	-	11,372
Benefits paid	(672,511)	(66,682)
<b>Fair value of plan assets at end of year</b>	<b>\$21,123,143</b>	<b>\$ -</b>
Funded status	\$ (176,491)	\$(5,279,158)
Employer contributions between measurement and statement date	-	-
<b>Funded status at year end</b>	<b>\$ (176,491)</b>	<b>\$(5,279,158)</b>
<b>Amounts Recognized in the Statement of Financial Position and Net Assets consist of:</b>		
Current liabilities	\$ -	\$ (73,828)
Noncurrent liabilities	(176,491)	(5,205,330)
<b>Net amount recognized in the Statement of Financial Position</b>	<b>\$ (176,491)</b>	<b>\$(5,279,158)</b>
<b>Amounts Recognized within the Statement of Activities consist of:</b>		
Net actuarial loss	\$ 726,745	\$ 145,911
Prior service cost	146,690	(11,650)
<b>Pension and postretirement benefit changes other than net periodic benefit costs</b>	<b>\$ 873,435</b>	<b>\$ 134,261</b>
<b>Accumulated Benefit Obligation end of year</b>	<b>\$18,649,635</b>	<b>\$ 5,279,158</b>

## Weighted-average Assumptions for Disclosure as of December 31, 2007

	<u>Pension Benefits</u>	<u>Other Postretirement Benefits</u>
Discount rate	6.25%	6.25%
Salary scale	4.00%	N/A
Health Care Cost Trend: Initial	N/A	10.00%
Health Care Cost Trend: Ultimate	N/A	5.00%
Year Ultimate Reached	N/A	2013

## Components of Net Periodic Benefit Cost and Other Amounts Recognized within the Statement of Activities

### Net Periodic Benefit Cost

Service cost	\$ 658,238	\$ 152,966
Interest cost	1,143,346	282,984
Expected return on plan assets	(1,600,377)	-
Recognized prior service cost	37,762	11,650
Recognized actuarial loss	138,600	-
<b>Net Periodic Benefit Cost</b>	<b>377,569</b>	<b>\$ 447,600</b>

### Other Changes in Plan Assets and Benefit Obligations Recognized within the Statement of Activities

Net actuarial gain	865,345	-
Recognized actuarial loss	(138,600)	-
Prior service cost	184,452	-
Recognized prior service cost	(37,762)	-
<b>Total recognized within the Statement of Activities</b>	<b>873,435</b>	<b>-</b>
<b>Total recognized in net benefit cost and within the Statement of Activities</b>	<b>\$ 1,251,004</b>	<b>-</b>

### Amounts Expected to be Recognized in Net Periodic Cost in the Coming Year

Loss recognition	\$ 210,155	\$ -
Prior service cost recognition	58,098	11,650
<b>Total</b>	<b>\$ 268,253</b>	<b>\$ 11,650</b>

### Effect of a 1% Increase in Trend on:

Benefit Obligation	N/A	\$ 944,037
Total Service Interest Cost	N/A	\$ 87,903

### Effect of a 1% Decrease in Trend on:

Benefit Obligation	N/A	\$ (800,830)
Total Service Interest Cost	N/A	\$ (72,988)

### Weighted-average Assumptions for Net Periodic Cost as of December 31, 2007

Discount rate	6.00%	6.00%
Expected asset return	8.00%	N/A
Salary scale	4.00%	N/A
Health Care Cost Trend: Initial	N/A	10.00%
Health Care Cost Trend: Ultimate	N/A	5.00%
Year Ultimate Reached	N/A	2012

For the pension plan the change in unrecognized net gain/loss is one measure of the degree to which important assumptions have coincided with actual experience. During 2007 the unrecognized net loss increased by 3.8% of the 12/31/2006 projected benefit obligation.

The discount rate was determined by projecting the plan's expected future benefit payments as defined for the projected benefit obligation, discounting those expected payments using a theoretical zero-coupon spot yield curve derived from a universe of high-

quality bonds as of the measurement date, and solving for the single equivalent discount rate that resulted in the same projected benefit obligation. A 1% increase/(decrease) in the discount rate would have (decreased)/increased the net periodic benefit cost for 2007 by (\$333,200)/\$322,700 and (decreased)/increased the year-end projected benefit obligation by (\$2.6)/\$2.9 million.

The expected return on the pension plan assets was determined based on historical and expected future returns of the various asset classes, using the target allocations described below.

### Pension Plan Assets

<u>Asset Category</u>	<u>Expected Long-Term Return</u>	<u>Target Allocation</u>	<u>Actual/Allocation 12/31/2007</u>
Equity securities	10.25%	60–70%	66%
Debt securities	4.50%	40–30%	34%
<b>TOTAL</b>	<b>8.00–8.50%</b>	<b>100%</b>	<b>100%</b>

### Estimated Future Benefit Payments

Estimated future benefit payments, including future benefit accrual	<b>Pension</b>	<b>Other Benefits</b>
2008	\$ 658,287	\$ 76,100
2009	\$ 813,638	\$ 110,100
2010	\$ 1,038,018	\$ 152,600
2011	\$ 1,151,061	\$ 174,500
2012	\$ 1,366,411	\$ 216,600
2013–2017	\$ 8,569,867	\$ 1,542,804

### Contributions

The company expects to contribute \$1,260,000 to the pension plan and \$76,100 to the postretirement benefit plan during 2008.

### Defined Contribution Plan

2007 SIPC contributions (60% of employee contributions, up to 3.6% of compensation)	\$ 130,244
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