COLONIAL BANCGROUP INC
Form 10-K
March 02, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2008

OR

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

For the transition period from _________ to _________

Commission File Number: 1-13508

THE COLONIAL BANCGROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**63-0661573**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
100 Colonial Bank Blvd.	
Montgomery, Alabama	**36117**

(Address of principal executive offices)	**(Zip Code)**

(334) 676-5000

(Registrant s telephone number, including area code.)

None

(Former name, former address and former fiscal year, if changed since last report)

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

Title of Class	**Name of each exchange on which registered**
Common Stock, $2.50 par value per share	**New York Stock Exchange**

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

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

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

Large accelerated filer x	Accelerated filer ¨	Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

As of June 30, 2008, the aggregate market value of the registrant s common stock held by non-affiliates of the registrant was $840,485,626, based on the closing price of $4.42 per share as reported on the New York Stock Exchange. (For purposes of calculating this amount, all directors, officers and principal shareholders of the registrant are treated as affiliates).

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	**Outstanding at February 18, 2009**
Common Stock, $2.50 par value per share	202,449,152 shares

DOCUMENTS INCORPORATED BY REFERENCE

Document	**Parts Into Which Incorporated**
Portions of Definitive Proxy Statement for 2009	Part III

Annual Meeting as specifically referred to herein

PART I

Item 1. ***Business***
General

The Registrant, The Colonial BancGroup, Inc. (BancGroup, Colonial or the Company) is a Delaware corporation organized in 1974 as a bank holding company under the Bank Holding Company Act of 1956, as amended (the BHCA). BancGroup was originally organized as Southland Bancorporation, and its name was changed in 1981. Pursuant to the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, BancGroup consolidated its various banking subsidiaries into Colonial Bank. Pursuant to the Gramm-Leach-Bliley Financial Services Modernization Act (Gramm-Leach), BancGroup elected to become a financial holding company which allows it to affiliate with securities firms and insurance companies and to engage in other activities that are financial in nature, incidental to such financial activities, or complementary to such activities.

The principal activity of BancGroup is to supervise and coordinate the business of its subsidiaries and to provide them with capital and services. BancGroup derives substantially all of its income from dividends received from Colonial Bank. Various statutory provisions and regulatory policies limit the amount of dividends Colonial Bank may pay without regulatory approval. In addition, federal statutes restrict the ability of Colonial Bank to make loans to BancGroup.

At December 31, 2008, BancGroup and its subsidiaries had 4,808 full-time equivalent employees. BancGroup s principal offices are located at 100 Colonial Bank Blvd., Montgomery, Alabama 36117, and its mailing address is: P.O. Box 241148, Montgomery, Alabama 36124. BancGroup s telephone number at its principal office is (334) 676-5000.

Subsidiary Bank

Colonial Bank was converted into an Alabama state-chartered non-member bank on June 10, 2008. Its legal name was changed to Colonial Bank. As of December 31, 2008, Colonial Bank had a total of 347 branches, with 197 branches in Florida, 90 branches in Alabama, 19 branches in Georgia, 21 branches in Texas and 20 branches in Nevada. Colonial Bank conducts a general commercial banking business in its respective service areas and offers a variety of demand, savings and time deposit products as well as extensions of credit through personal, commercial and mortgage loans within each of its market areas. Colonial Bank also provides additional services to its markets through wealth management services, electronic banking services and credit card services. Through its wealth management area, Colonial Bank s wholly owned subsidiaries, Colonial Investment Services, Inc., Colonial Investment Services of Florida, Georgia, Nevada and Tennessee offer various insurance products and annuities for sale to the public. These subsidiaries are regulated by each state s department of insurance.

Colonial Bank encounters intense competition in its commercial banking business, generally from other banks located in its respective metropolitan and service areas. Colonial Bank competes for interest bearing funds with other banks and with many non-bank issuers of securities. Competition also exists with banks in other metropolitan areas of the United States, many of which are larger in terms of capital resources and personnel. In the conduct of certain aspects of its commercial banking business, Colonial Bank competes with savings and loan associations, credit unions, mortgage banks, factors, insurance companies and other financial institutions. At December 31, 2008, Colonial Bank accounted for approximately 99.3% of BancGroup s consolidated assets.

Other Financial Services Operations

BancGroup s subsidiary Colonial Brokerage, Inc., a Delaware corporation, provides full service and discount brokerage services and investment advice and is a member of and is regulated by the Financial Industry Regulatory Authority.

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Executive Overview of Operations and Condition

The financial services industry in the United States is operating today in an exceptionally difficult, uncertain and rapidly changing environment presenting risks that are difficult to assess and quantify. As of December 31, 2008, BancGroup and Colonial Bank met all applicable regulatory requirements relating to capital. For the year ended December 31, 2008, however, BancGroup reported a net loss of $880.5 million (including a net goodwill impairment charge of $534.4 million) compared to net income of $180.9 million in 2007. During 2008, Colonial charged off $642.8 million of loans and recorded a provision for loan losses of $728.9 million, representing substantial increases over the 2007 net charge-offs of $54.1 million and a loan loss provision of $106.5 million. The results of operations and financial condition of BancGroup and Colonial Bank led to increased regulatory scrutiny during the fourth quarter.

Because of continued economic uncertainty, the Company elected to apply for participation in the U.S. Treasury Department s Capital Purchase Program (TARP). During the fourth quarter of 2008, the Company received preliminary approval to issue a maximum of $553 million of TARP preferred stock to the U.S. Treasury Department. The preliminary approval is subject to certain conditions, including the raising of $300 million in additional capital from unaffiliated parties. As of December 31, 2008, the maximum amount of TARP preferred stock the Company could issue would be approximately $536 million.

Since receiving preliminary approval, the Company has pursued a number of capital-raising alternatives. On January 27, 2009, SunTx Capital Partners (SunTx) of Dallas, Texas, signed a non-binding letter of intent with BancGroup relating to a potential investment by SunTx and prospective co-investors of up to 24.9% of the Company s proforma capitalization, subject to the negotiation of a definitive agreement, completion of due diligence and obtaining the necessary approvals. In addition, BancGroup is currently in discussions with other third parties regarding potential investments in or other transactions with the Company. The current condition of the banking industry and the overall uncertainty in financial markets have negatively impacted Colonial s capital raising efforts. No assurances can be given that the Company will be able to raise the capital necessary to satisfy the conditions of the TARP preliminary approval or as to the price, terms or structure of any such transactions.

BancGroup s common stock has recently traded below $1 per share. Raising $300 million of additional capital through the sale of common equity interests at current prices would therefore dilute existing shareholders to a minority position. Moreover, in the event BancGroup is not successful in raising additional capital in the near term, both Colonial Bank and BancGroup would likely become subject to even greater regulatory supervision, which could result in additional restrictions. Although the New York Stock Exchange, on which BancGroup s stock is traded, has recently announced a proposed temporary suspension through June 30, 2009 of its stock-price rule, the Exchange s existing rules require that a listed company s stock trade at or above $1 per share.

The preceding discussion is only a brief summary of the Company s condition, results of operations and regulatory categorization and should be read in conjunction with *Risk Factors*, *Legal Proceedings, Management s Discussion and Analysis of Financial Condition and Results of Operations, Consolidated Financial Statements* and the *Notes to Consolidated Financial Statements*.

Segment Information

The Company has six reportable segments for management reporting five regional bank segments located in Florida, Alabama, Georgia, Nevada and Texas, and the mortgage warehouse segment headquartered in Orlando, Florida. Each regional bank segment consists of commercial lending and full service branches in its geographic region. The branches provide a full range of traditional banking products as well as wealth management and mortgage banking services. The mortgage warehouse segment provides financing collateralized by residential mortgage loans and other services to mortgage origination companies. Corporate functions not included in these reportable segments include treasury and parent activities, back office operations and intercompany eliminations. These functions are reported together as Corporate/Treasury/Other. For additional information related to segments, see Note 27, *Segment Information*, in the Notes to Consolidated Financial Statements.

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Available Information

BancGroup makes available, free of charge through its Internet website (www.colonialbank.com), the Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to these reports filed or furnished pursuant to Section 13(a) of the Exchange Act as soon as reasonably practicable after electronically filing or furnishing such material with the Securities and Exchange Commission.

Regulatory Environment

The following is a brief summary of the regulatory environment in which BancGroup and Colonial Bank operate and is not designed to be a complete discussion of all statutes and regulations affecting such operations, including those statutes and regulations specifically mentioned herein. Changes in the laws and regulations applicable to BancGroup and Colonial Bank can affect the operating environment in substantial and unpredictable ways. BancGroup cannot accurately predict whether legislation will ultimately be enacted, and if enacted, what the ultimate effect that legislation would have on BancGroup or its subsidiaries financial condition or results of operations. While banking regulations are material to the operations of BancGroup and Colonial Bank, it should be noted that supervision, regulation and examination of BancGroup and Colonial Bank are intended primarily for the protection of depositors, not security holders.

BancGroup is a registered bank holding company and a financial holding company subject to supervision and regulation by the Board of Governors of the Federal Reserve System (Federal Reserve). As such, it is subject to the Bank Holding Company Act (BHCA) and many of the Federal Reserve s regulations promulgated thereunder. The Federal Reserve has broad enforcement powers over bank holding companies, including the power to impose substantial fines and civil money penalties.

Colonial Bank converted from a national banking association subject to supervision and examination by the Office of the Comptroller of the Currency (OCC) to an Alabama state-chartered bank on June 10, 2008, subject to supervision and examination by the Alabama State Banking Department and the Federal Deposit Insurance Corporation (FDIC). To the extent provided by law, the deposits of Colonial Bank are insured by the FDIC. The FDIC assesses deposit insurance premiums, the amount of which may, in the future, depend in part on the condition of Colonial Bank. Moreover, the FDIC may terminate deposit insurance of Colonial Bank under certain very limited circumstances. The bank regulatory agencies have broad enforcement powers over depository institutions under their jurisdiction, including the power to terminate deposit insurance, to impose fines and other civil and criminal penalties and to appoint a conservator or receiver if any of a number of conditions are met.

Current Regulatory Matters

Due to their current condition and results of operations, BancGroup and Colonial Bank are operating under heightened regulatory scrutiny and have been and will be taking steps which are expected to improve their asset quality and capital. Colonial Bank entered into an informal Memorandum of Understanding (the Bank MOU) with the FDIC and the Alabama State Banking Department on December 15, 2008, and BancGroup entered into an informal Memorandum of Understanding (the BancGroup MOU) with the Federal Reserve Bank of Atlanta on January 6, 2009. Neither the Bank MOU nor the BancGroup MOU is considered to be a written agreement pursuant to Section 8 of the FDI Act.

Key elements of the Bank MOU include: improvement of regulatory capital ratios to an 8% Tier I leverage ratio and a 12% total risk-based capital ratio by March 31, 2009; reduction in classified asset levels by dates beginning June 30, 2009; enhancement of the Company s credit process and prior regulatory approval for the payment of dividends on Colonial Bank common stock.

Key elements of the BancGroup MOU include: utilization of holding company resources to support Colonial Bank in meeting the requirements of the Bank MOU and prior regulatory approval for the issuance of debt, payment of BancGroup dividends, or purchase or redemption of treasury stock.

As of December 31, 2008, Colonial Bank maintained capital sufficient to meet the minimum capital levels to be categorized as well capitalized under the regulatory framework for prompt corrective action.

The attainment of the targeted capital ratios included in the Bank MOU will require either (1) a significant increase in Colonial Bank s capital, or (2) a substantial decrease in Colonial Bank s asset levels. One means of achieving the significant increase to Colonial Bank s capital is the issuance of preferred stock under the U.S. Treasury Department s Capital Purchase Program. As discussed under *Risk Factors*, Colonial s final approval to sell preferred stock to the U.S. Treasury Department is contingent upon Colonial raising additional capital of $300 million and the closing conditions set forth in the final definitive agreements.

These matters are a major focus of the attention and efforts of the Board of Directors and management.

Mergers, Acquisitions and Changes in Control

One limitation under the BHCA and the Federal Reserve s regulations requires that BancGroup obtain prior approval of the Federal Reserve before BancGroup acquires, directly or indirectly, more than 5% of any class of voting securities of another bank. Prior approval also must be obtained before BancGroup acquires all or substantially all of the assets of another bank, or before it merges or consolidates with another bank holding company. Because BancGroup is a registered bank holding company, persons seeking to acquire 25% or more of any class of its voting securities must receive the prior approval of the Federal Reserve. Similarly, under certain circumstances, persons seeking to acquire between 5% and 25% also may be required to obtain prior Federal Reserve approval.

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, among other things, amended the BHCA to permit bank holding companies, subject to certain limitations, to acquire either control or substantial assets of a bank located in states other than that bank holding company s home state regardless of state law prohibitions. In addition, this legislation also amended the Federal Deposit Insurance Act to permit the merger of insured banks with banks in other states, subject to certain limitations.

FDIC Improvement Act

As a result of enactment of the FDIC Improvement Act (FDICIA) in 1991, banks are subject to increased reporting requirements and more frequent examinations by the bank regulatory agencies. The agencies also have the authority to dictate certain key decisions that formerly were left to management, including, but not limited to, compensation standards, loan underwriting standards, asset growth and payment of dividends. Failure to comply with these standards, or failure to maintain capital above specified levels set by the regulators, could lead to the imposition of penalties or the forced resignation of management. If a bank becomes critically undercapitalized, the banking agencies have the authority to place the institution into receivership.

Consumer Protection Laws

There are a number of laws that govern the relationship between Colonial Bank and its customers. For example, the Community Reinvestment Act (CRA) is designed to promote the offering of products and services to low and moderate income persons and to businesses within the Bank s assessment areas. The Home Mortgage Disclosure Act and the Equal Credit Opportunity Act attempt to minimize lending decisions based on impermissible criteria, such as race or gender. The Truth-in-Lending Act and the Truth-in-Savings Act require banks to provide certain disclosure of relevant terms related to loans and deposit accounts, respectively. Anti-tying restrictions (which prohibit, for instance, conditioning the availability or terms of credit on the purchase of another banking product) further restrict Colonial Bank s relationships with its customers.

Gramm-Leach-Bliley Financial Services Modernization Act (GLBA)

GLBA became effective in March 2000. The primary purpose of GLBA was to eliminate barriers between investment banking and commercial banking and to permit, within certain limitations, the affiliation of financial service providers. Generally, GLBA: (i) repealed the historical restrictions against, and eliminated many federal and state law barriers to affiliations among banks, securities firms, insurance companies and other financial service providers; (ii) provided a uniform framework for the activities of banks, savings institutions and their holding companies; (iii) broadened the activities that may be conducted by and through national banks and other banking subsidiaries of bank holding companies; (iv) provided an enhanced framework for protecting the privacy of consumers information; (v) adopted a number of provisions related to the capitalization, membership, corporate governance and other measures designed to modernize the Federal Home Loan Bank System; (vi) modified the laws governing the implementation of the CRA; and (vii) addressed a variety of other legal and regulatory issues affecting both day-to-day operations and long-term activities of financial institutions.

More specifically, under GLBA, bank holding companies, such as BancGroup, that meet certain management, capital and CRA standards, are permitted to become financial holding companies and, by doing so, to affiliate with securities firms and insurance companies and to engage in other activities that are financial in nature, incidental to such financial activities or complementary to such activities. A bank holding company may become a financial holding company if each of its subsidiary banks is well capitalized under the FDICIA prompt corrective action provisions, is well managed and has at least a satisfactory rating under the CRA. The required filing is a declaration that the bank holding company wishes to become a financial holding company and meets all applicable requirements. BancGroup became a financial holding company on May 12, 2000.

Generally, no prior regulatory approval will be required for a financial holding company to acquire a company, other than a bank or savings association, engaged in activities permitted under GLBA. Activities cited by GLBA as being financial in nature include:

- securities underwriting, dealing and market making;
- sponsoring mutual funds and investment companies;
- insurance underwriting and agency;
- merchant banking activities; and
- activities that the Federal Reserve has determined to be closely related to banking.

Privacy Laws

In 2000, the federal banking regulators issued final regulations implementing certain provisions of GLBA governing the privacy of consumer financial information. The regulations limit the disclosure by financial institutions, such as BancGroup, Colonial Bank and certain of their subsidiaries, of nonpublic personal information about individuals who obtain financial products or services for personal, family or household purposes. Subject to certain exceptions allowed by law, the regulations cover information sharing between financial institutions and nonaffiliated third parties. More specifically, the regulations require financial institutions to (i) provide initial notices to customers about their privacy policies, describing the conditions under which they may disclose nonpublic personal financial information to nonaffiliated third parties and affiliates; (ii) provide annual notices of their privacy policies to their current customers; and (iii) provide a reasonable method for customers to opt-out of disclosures to nonaffiliated third parties.

The Fair Credit Reporting Act (FCRA) governs the ability of a financial institution to share customer financial information with its affiliates. The FCRA requires financial institutions to provide their customers with notice and an opportunity to opt-out before sharing certain information with its affiliates. In December 2003, the Fair and Accurate Credit Transactions Act of 2003 (FACTA) was enacted. FACTA includes a provision further limiting a financial institution s ability to share customer information with its affiliates for marketing purposes by requiring financial institutions to provide their customers with the ability to opt-out of such sharing of customer information. Regulations implementing this provision of FACTA had a mandatory effective date of October 1, 2008. FACTA section 114, which requires institutions to develop and implement a written program to detect, prevent and mitigate identity theft for certain new and existing accounts, was required to be in place by November 1, 2008.

Protection of Customer Information

In February 2001, the federal banking regulators issued final regulations implementing the provisions of GLBA relating to the protection of customer information. The regulations, applicable to financial institutions, like Colonial Bank, and certain of their nonbank subsidiaries, and to bank holding companies, like BancGroup, and certain of their nonbank subsidiaries, relate to administrative, technical, and physical safeguards for customer records and information. These safeguards are intended to: (i) ensure the security and confidentiality of customer records and information; (ii) protect against any anticipated threats or hazards to the security or integrity of such records; (iii) protect against unauthorized access to or use of such records or information that could result in substantial harm or inconvenience to any customer; and (iv) ensure the proper disposal of such information.

In March 2005, the federal banking agencies jointly issued Interagency Guidance on Response Programs for Unauthorized Access to Customer Information and Customer Notice. The guidance requires all financial institutions to implement a response program to address security breaches involving customer information. The guidance requires a financial institution s response to include, among other things, procedures for notifying customers about incidents of unauthorized access when certain criteria are met.

Bank Secrecy Act

The Bank Secrecy Act (BSA) is a tool the U.S. government uses to fight drug trafficking, money laundering and other crimes. Under the BSA, financial institutions are required to file certain reports, including suspicious activities reports and currency transaction reports, with the Financial Crimes Enforcement Network under certain circumstances. Financial institutions are also required to have policies and procedures in place to ensure compliance with the BSA. If a financial institution fails to timely file a report or fails to implement its BSA policies and procedures, it could subject the institution to enforcement action or civil money penalties. In July 2007, federal banking regulators issued the Interagency Statement on Enforcement of Bank Secrecy Act/Anti- Money Laundering Requirements to provide greater consistency among the agencies in enforcement decisions in BSA matters and to offer insight into the considerations that form the basis of such BSA enforcement decisions.

On October 26, 2001, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT Act) was signed into law. The USA PATRIOT Act amended the BSA and broadened the application of anti-money laundering regulations to apply to additional types of financial institutions, such as broker-dealers, and strengthened the ability of the U.S. government to detect and prosecute international money laundering and the financing of terrorism. The principal provisions of Title III of the USA PATRIOT Act require that regulated financial institutions: (i) establish an anti-money laundering program that includes training and audit components; (ii) comply with regulations regarding the verification of the identity of any person seeking to open an account; (iii) take additional required precautions with non-U.S. owned accounts; and (iv) perform certain verification and certification of money laundering risk for their foreign correspondent banking relationships. The USA PATRIOT Act also expanded the conditions under which funds in a U.S. interbank account may be subject to forfeiture and increased the penalties for violation of anti-money laundering regulations. Failure of a financial institution to comply with the USA PATRIOT Act s requirements could have serious legal and reputational consequences for the institution. BancGroup has adopted policies, procedures and controls to address compliance with the requirements of the USA PATRIOT Act under the existing regulations and will continue to revise and update its policies, procedures and controls to reflect changes required by the USA PATRIOT Act and implementing regulations.

Safety and Soundness Standards

Pursuant to FDICIA, the federal banking regulatory agencies have adopted a set of guidelines prescribing safety and soundness standards for depository institutions such as Colonial Bank. The guidelines establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, asset quality, earnings and compensation, fees and benefits. In general, the guidelines require, among other things, appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director or principal shareholder. In addition, the agencies adopted regulations that authorize an agency to order an institution that has been given notice by an agency that it is not satisfying any of such safety and soundness standards to submit a compliance plan. If the institution fails to submit an acceptable compliance plan or fails to implement an accepted plan, the agency must issue an order directing action to correct the deficiency and may issue an order directing other actions be taken, including restricting asset growth, restricting interest rates paid on deposits, and requiring an increase in the institution s ratio of tangible equity to assets.

Payment of Dividends and Other Restrictions

BancGroup is a legal entity separate and distinct from its subsidiaries, including Colonial Bank. There are various legal and regulatory limitations on the extent to which BancGroup s subsidiaries can, among other things, finance, or otherwise supply funds to, BancGroup. There are legal restrictions under federal and state law on the payment of dividends by banks. The relevant regulatory agencies also have authority to prohibit BancGroup and Colonial Bank from engaging in what, in the opinion of such regulatory body, constitutes an unsafe or unsound banking practice. The payment of dividends could, depending upon the financial condition of BancGroup and Colonial Bank, be deemed to constitute such an unsafe or unsound practice. As previously discussed, both Colonial Bank and BancGroup are required to receive prior regulatory approval for the payment of dividends on common stock.

In addition, Colonial Bank and its subsidiaries are subject to limitations under Sections 23A and 23B of the Federal Reserve Act with respect to extensions of credit to, investments in, and certain other transactions with, BancGroup and its other subsidiaries. Furthermore, loans and extensions of credit are also subject to various collateral requirements. The Federal Reserve has adopted Regulation W, which combines the Federal Reserve s interpretations and exemptions relating to Sections 23A and 23B of the Federal Reserve Act.

Capital Adequacy

The Federal Reserve has adopted regulations which provide for minimum risk-based and leverage capital guidelines for bank holding companies. The minimum required ratio of total capital to risk-weighted assets (including certain off-balance sheet items, such as standby letters of credit) is 8%, of which 4% must consist of Tier I capital. The minimum required leverage capital ratio is 3% for bank holding companies that meet certain specified criteria, including that they have the highest regulatory rating. A minimum leverage ratio of 4% is required for bank holding companies not meeting these criteria. Generally, bank holding companies are expected to operate well above the minimum capital ratios. Higher capital ratios may be required for any bank holding company if warranted by its particular circumstances or risk profile. Failure to meet capital guidelines can subject a bank holding company to a variety of formal and informal enforcement remedies, including restrictions on its operations and activities.

Regarding depository institutions, the prompt corrective action provisions of the federal banking statutes establish five capital categories (well capitalized , adequately capitalized , undercapitalized , significantly undercapitalized and critically undercapitalized), and impose significant restrictions on the operations of an institution that is not at least adequately capitalized. To be considered well capitalized, an institution must maintain a ratio of total capital to risk weighted assets of at least 10% of which 6% must consist of Tier I capital as well as a Tier I leverage ratio of at least 5%. To be considered adequately capitalized, the institution must maintain those same capital ratios at levels equal to or exceeding 8%, 4% and 4%, respectively. Under certain circumstances, an institution may be downgraded to a category lower than that warranted by its capital levels and subjected to the supervisory restrictions applicable to institutions in the lower capital category. As of December 31, 2008, Colonial Bank met the minimum capital levels to be categorized as well capitalized under the regulatory framework for prompt corrective action. See specific discussion of Colonial Bank s and BancGroup s capital adequacy as previously discussed under *Current Regulatory Matters*.

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An undercapitalized depository institution is subject to restrictions in a number of areas, including capital distributions, payments of management fees and expansion. In addition, an undercapitalized depository institution is required to submit a capital restoration plan. A depository institution s holding company must guarantee the capital plan up to an amount equal to the lesser of 5% of the depository institution s assets at the time it becomes undercapitalized or the amount needed to restore the capital of the institution to the levels required for the institution to be classified as adequately capitalized at the time the institution fails to comply with the plan. A depository institution is treated as if it is significantly undercapitalized if it fails in any material respect to implement a capital restoration plan.

Significantly undercapitalized depository institutions may be subject to a number of additional significant requirements and restrictions, including requirements to sell sufficient voting stock to become adequately capitalized, to improve management, to restrict asset growth, to prohibit acceptance of correspondent bank deposits, to restrict senior executive compensation and to limit transactions with affiliates. Critically undercapitalized depository institutions are further subject to restrictions on paying principal or interest on subordinated debt, making investments, expanding, acquiring or selling assets, extending credit for highly-leveraged transactions, paying excessive compensation, amending their charters or bylaws and making any material changes in accounting methods. In general, a receiver or conservator must be appointed for a depository institution within 90 days after the institution is deemed to be critically undercapitalized.

Support of Subsidiary Bank

Under Federal Reserve policy, BancGroup is expected to act as a source of financial strength to, and to commit resources to support, Colonial Bank. This support may be required at times when, absent such Federal Reserve policy, BancGroup might not otherwise be inclined to provide it. In the event of a bank holding company s bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to priority of payment.

FDIC Insurance Assessments

The FDIC is an independent federal agency established originally to insure the deposits, up to prescribed statutory limits, of federally insured banks and to preserve the safety and soundness of the banking industry. The FDIC has adopted a risk-based assessment system for insured depository institutions that takes into account the risks attributable to different categories and concentrations of assets and liabilities.

Colonial Bank s deposit accounts are insured by the FDIC to the maximum extent permitted by law. Colonial Bank pays deposit insurance premiums to the FDIC based on a risk-based assessment system established by the FDIC for all insured institutions. Institutions considered well-capitalized and financially sound pay the lowest premiums, while those institutions that are less than adequately capitalized and of substantial supervisory concern pay the highest premiums. During 2008, assessment rates for insured institutions ranged from 5 cents per $100 of assessable deposits for well-capitalized institutions with minor supervisory concerns to 43 cents per $100 of assessable deposits for undercapitalized institutions with substantial supervisory concerns. In 2009, assessment rates are expected to range between 12 and 50 cents per $100 of assessable deposits for the first quarter and 8 and 77.5 cents per $100 of assessable deposits for the remainder of the year. The large premium increase is due to the Emergency Economic Stabilization Act of 2008 and the Temporary Liquidity Guarantee Program, both of which increased the deposit insurance coverage available to Colonial s depositors.

Emergency Economic Stabilization Act of 2008. In October 2008, the Emergency Economic Stabilization Act of 2008 (EESA) was signed into law. The EESA temporarily revises the federal deposit insurance laws by increasing the basic deposit insurance coverage from $100,000 to $250,000 per depositor. This revision is currently effective through December 31, 2009.

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Temporary Liquidity Guarantee Program. In order to promote financial stability in the economy, the FDIC adopted the Temporary Liquidity Guarantee Program (TLGP) on October 13, 2008. Participation in the program is voluntary. However, once participation is elected, it can not be revoked. Colonial has chosen to participate in the Transaction Account Guarantee Program component of the TLGP. Under the Transaction Account Guarantee Program, the FDIC will fully insure funds held in noninterest-bearing transaction accounts. Noninterest-bearing transaction accounts are ones that do not accrue or pay interest and for which the institution does not require an advance notice of withdrawal. Also covered are interest on lawyers trust accounts (IOLTA) and negotiable order of withdrawal (NOW) accounts with interest rates lower than 50 basis points. These revisions are only effective through December 31, 2009.

Federal Deposit Insurance Reform Act of 2005. In February 2006, the Federal Deposit Insurance Reform Act of 2005 and the Federal Deposit Insurance Reform Conforming Amendments Act of 2005 (collectively, the Reform Act) were signed into law. The Reform Act revised the laws concerning federal deposit insurance by making the following changes: (i) merging the Bank Insurance Fund and the Savings Association Insurance Fund into a new fund, the Deposit Insurance Fund (DIF), effective March 31, 2006; (ii) increasing the deposit insurance coverage for certain retirement accounts to $250,000 effective April 1, 2006; (iii) beginning in 2010, deposit insurance coverage on individual accounts may be indexed for inflation; (iv) the FDIC will have more discretion in managing deposit insurance assessments; and (v) eligible institutions will receive a one-time initial assessment credit.

The Reform Act authorized the FDIC to revise the risk-based assessment system. Accordingly, insurance premiums are based on a number of factors, including the risk of loss that insured institutions pose to the DIF. The Reform Act replaced the minimum reserve ratio of 1.25% with a range of between 1.15% and 1.50% for the DIF, depending on projected losses, economic changes and assessment rates at the end of each calendar year. In addition, the FDIC is no longer prohibited from charging banks in the lowest risk category when the reserve ratio premium is greater than 1.25%.

In November 2006, the FDIC adopted changes to its risk-based assessment system. Under the new system, the FDIC will evaluate an institution s risk based on supervisory ratings for all insured institutions, financial ratios for most institutions and long-term debt issuer ratings for certain large institutions.

In addition to deposit insurance assessments, the FDIC is authorized to collect assessments against insured deposits to be paid to the Finance Corporation (FICO) to service FICO debt incurred during the 1980 s. The FICO assessment rate is adjusted quarterly. The average annual assessment rate in 2008 was 1.12 cents per $100 for insured deposits. For the first quarter of 2009, the FICO assessment rate for such deposits will be 1.14 cents per $100 of assessable deposits.

Alabama State Banking Department Assessment

The Alabama State Banking Department imposes a quarterly assessment on all state banks under its supervision. The amount of the quarterly assessment is based on the bank s total assets at the end of the prior quarter. Colonial Bank s state assessment expense for the year ended December 31, 2008 was $1.2 million. Prior to Colonial Bank converting to a state-chartered bank on June 10, 2008, Colonial paid assessments to the OCC totaling $1.6 million for the first half of 2008. No assessment was paid to the OCC for the second half of the year.

Other Subsidiary Regulation

Certain subsidiaries of BancGroup and Colonial Bank are regulated by other governmental agencies. Where material, such regulation is disclosed with the disclosure of the subsidiary.

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Additional Information

Additional information, including statistical information concerning the business of BancGroup, is set forth herein. See *Selected Financial Data* and *Selected Quarterly Financial Data 2008-2007* and *Management s Discussion and Analysis of Financial Condition and Results of Operations*.

Executive Officers and Directors

Pursuant to general instruction G, information regarding executive officers of BancGroup is contained herein at Item 10.

Item 1A. *Risk Factors*
Industry Factors

As a financial services company, our business and earnings are significantly affected by general business and economic conditions, particularly in the real estate industry, and accordingly, our business and earnings could be further harmed in the event of a continuation or deepening of the current U.S. recession or further market deterioration or disruption.

Our business and earnings are sensitive to general business, economic and market conditions in the United States. These conditions include changes in short-term and long-term interest rates, inflation, deflation, fluctuation in the real estate and debt capital markets, developments in national and regional economies and changes in government policies and regulations.

Our business and earnings are particularly sensitive to economic and market conditions affecting the real estate industry because most of our loan portfolio consists of commercial real estate, construction and residential loans. While generally containing lower risk than unsecured loans, commercial real estate and construction loans generally involve higher credit risk than conventional single-family residential loans. Such loans also generally involve larger individual loan balances. In addition, real estate construction loans may be affected to a greater extent than residential loans by adverse conditions in real estate markets or the economy because many real estate construction borrowers ability to repay their loans is dependent on successful development of their properties, as well as the factors affecting residential real estate borrowers. Risk of loss on a construction loan depends largely upon whether the initial estimate of the property s value at completion of construction equals or exceeds the cost of property construction (including interest) and the availability of permanent take-out financing. During the construction phase, a number of factors can result in delays and cost overruns. Construction and commercial real estate loans also involve greater risk because they may not be fully amortizing over the loan period, but have a balloon payment due at maturity. A borrower s ability to make a balloon payment may depend on the borrower being able to refinance the loan, timely sell the underlying property or liquidate other assets.

The current U.S. recession has resulted in a reduction in the value of the real estate assets securing a large portion of the loans that we hold. An increasing number of borrowers have become delinquent or defaulted on their loans, thereby adversely affecting our results of operations and financial condition, including the value of our intangible assets. A further increase in the number of delinquencies or defaults would result in higher levels of nonperforming assets, net charge-offs and provision for loan losses, adversely affecting our results of operations and financial condition.

The condition of the residential mortgage and related markets and the economy may deteriorate further and adversely affect our business.

Recently, the residential mortgage market in the United States has experienced a variety of worsening economic conditions that have adversely affected the performance and market value of our residential construction and mortgage loans. Across the United States, delinquencies, foreclosures and losses with respect to residential construction and mortgage loans generally have increased and may continue to increase. In addition, housing prices and appraisal values in most markets have declined or stopped appreciating. An extended period of flat or declining housing values may result in additional increases in delinquencies and further losses on residential construction and mortgage loans.

Our earnings are significantly affected by the fiscal and monetary policies of the federal government and its agencies.

The Board of Governors of the Federal Reserve System regulates the supply of money and credit in the United States. Its policies determine in large part our cost of funds for lending and investing and the return we earn on those loans and investments, both of which impact our net interest margin, and can materially affect the value of financial instruments we hold, such as debt securities. Its policies also can affect our borrowers, potentially increasing the risk that they may fail to repay their loans. Changes in Federal Reserve Board policies are beyond our control and difficult to predict or anticipate.

The financial services industry is highly competitive.

We operate in a highly competitive industry which has become even more competitive as a result of legislative, regulatory and technological changes and continued consolidation. Banks, securities firms and insurance companies can now merge by creating a financial services company called a financial holding company, which can offer virtually any type of financial service, including banking, securities underwriting, insurance (both agency and underwriting) and merchant banking. A number of foreign banks have acquired financial services companies in the United States, further increasing competition in the U.S. market. Also, technology has lowered barriers to entry and made it possible for nonbanks to offer products and services traditionally provided by banks, such as automatic transfer and automatic payment systems. Many of our competitors have fewer regulatory constraints and some have lower cost structures. Many nonbanks have converted to bank holding companies in order to receive government assistance under the U.S. Treasury Department s Capital Purchase Program (TARP). The newly formed bank holding companies are expected to increase competition for deposits and other business traditionally pursued by banks.

The financial services industry is heavily regulated by federal and state agencies.

The Company, its subsidiary bank and certain nonbank subsidiaries are heavily regulated by federal and state agencies. This regulation is to protect depositors, federal deposit insurance funds and the banking system as a whole, not security holders. Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect us in substantial and unpredictable ways including limiting the types of financial services and products we may offer and/or increasing the ability of nonbanks to offer competing financial services and products. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies and damage to our reputation. For more information, refer to discussions of regulatory considerations contained in Item 1 *Business* and Note 19, *Regulatory Matters and Restrictions.*

The Emergency Economic Stabilization Act of 2008 (EESA) and the American Recovery and Reinvestment Act of 2009 (ARRA) may not stabilize the financial services industry or the U.S. economy.

The EESA was signed into law on October 3, 2008. The legislation was intended to alleviate the financial crisis affecting the U.S. banking system. A number of programs have been and are being developed and implemented under EESA. The EESA may not have the intended effect and therefore the condition of the financial services industry may worsen instead of improve. The failure of the EESA to improve the condition of the U.S. banking system could significantly adversely impact our business, our financial condition, our financial results, our access to funding or capital as well as the trading price of our common stock or other instruments.

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The ARRA was signed into law on February 17, 2009. The legislation was intended to provide immediate and long-term solutions to the current U.S. recession. The ARRA may not have the intended effect; therefore, the current U.S. recession and the condition of the financial services industry may worsen instead of improve. The failure of the ARRA to improve the current U.S. recession and/or improve the condition of the U.S. banking system could significantly adversely impact our business, our financial condition, our financial results, or our access to funding or capital, as well as the trading price of our common stock or other instruments.

Current market volatility and industry developments may adversely affect our business and financial results.

The volatility in the capital and credit markets along with the housing declines during the last year have resulted in significant pressure on the financial services industry. We have experienced a higher level of foreclosures and higher losses upon foreclosure than we have historically. If current volatility and market conditions continue or worsen, there can be no assurance that our industry, results of operations or our business will not continue to be significantly adversely impacted. We may have further increases in loan losses, deterioration of capital or limitations on our access to funding or capital, if needed.

Further, if other financial institutions fail to be adequately capitalized or funded, it may negatively impact our business and financial results. We routinely interact with numerous financial institutions in the ordinary course of business and are therefore exposed to operational and credit risk to those institutions. Failures of such institutions may significantly adversely impact our operations.

Strategies to manage interest rate risk may yield results other than those anticipated.

Changes in the interest rate environment are difficult to predict. Net interest margins can expand or contract which can significantly impact our overall earnings. Changes in interest rates can also adversely affect how we apply critical management estimates, our projected returns on investments, as well as the determination of fair values of certain assets.

Events such as natural disasters, acts of terrorism or war occurring in the U.S. could affect our business and financial results.

Our business and earnings are sensitive to general business, economic and market conditions occurring in the U.S. and particularly in our primary markets. Events such as natural disasters, a terrorist attack or war could result in prolonged business disruption and/or materially impair the value of collateral securing loans, which could adversely impact our business.

Company Factors

The impact on us of recently enacted legislation, in particular the Emergency Economic Stabilization Act of 2008 (EESA), the American Recovery and Reinvestment Act of 2009 (ARRA), and their implementing regulations, and actions by the FDIC, cannot be predicted at this time.

The programs established or to be established under the EESA, ARRA and Troubled Asset Relief Program are evolving and may have adverse effects on us. We may face increased regulation of our industry. Compliance with such regulation may increase our costs and limit our ability to pursue business opportunities. Also, participation in specific programs may subject us to additional restrictions. For example, participation in the Troubled Asset Relief Program will limit (without the consent of the U.S. Treasury Department) our ability to pay a dividend on common stock or to repurchase our common stock for so long as any securities issued under such program remain outstanding. It will also subject us to additional executive compensation restrictions. Similarly, programs established by the FDIC under the systemic risk exception of the Federal Deposit Act, may have an adverse effect on us, whether or not we participate in the programs. Participation in the FDIC Temporary Liquidity Guarantee Program requires the payment of additional insurance premiums to the FDIC based upon the increased deposit coverage afforded thereunder. Further, we will be required to pay significantly higher Federal

Deposit Insurance Corporation premiums because market developments have decreased the insurance fund of the FDIC and reduced the ratio of reserves to insured deposits. The full effects of these various programs cannot reliably be determined at this time.

Failure to receive final approval for participation in the U.S. Treasury Department s Capital Purchase Program (TARP) or our inability to raise additional capital on terms and conditions that are satisfactory to us could have a significant impact on our Company.

During the fourth quarter of 2008, we received preliminary approval from the U.S. Treasury Department to participate in its Capital Purchase Program subject to raising additional capital of at least $300 million. The amount of TARP preferred stock to be issued is subject to a maximum of 3% of our latest bank holding company total risk weighted assets. As of December 31, 2008, if all conditions are satisfied the maximum amount of TARP preferred stock we would expect to issue to the U.S. Treasury Department is approximately $536 million. The preliminary approval also includes provisions concerning the timely completion of the preferred stock agreements by Colonial, which time has since elapsed. BancGroup has been informed by a representative of the U.S. Treasury Department that the Company will be allowed additional time to satisfy the conditions contained in the preliminary approval. The preliminary approval also contains other provisions which, along with the time constraints, would allow the U.S. Treasury Department to modify or revoke the preliminary approval. While we are actively pursuing a variety of capital raising alternatives to satisfy the preliminary approval conditions to issue TARP preferred stock, we cannot guarantee our success, and therefore we may not receive additional third party capital or issue TARP preferred stock, and could therefore be subject to increased regulatory oversight pursuant to the MOUs discussed in Item 1 and in these Risk Factors below. Failure to adequately address the regulatory concerns in these informal MOUs may result in actions by our banking regulators under the prompt corrective action provisions ranging from a formal written agreement pursuant to Section 8 of the FDIC Improvement Act which would preclude Colonial Bank from being considered well capitalized to the restriction or prohibition of certain activities by BancGroup or Colonial Bank. If Colonial Bank were to be deemed an undercapitalized institution, the banking regulators could require the Bank to submit a plan for restoring Colonial Bank to an acceptable capital category and our failure to adequately comply could eventually allow the banking regulators to appoint a receiver or conservator of Colonial Bank s net assets.

The issuance of preferred stock and convertible warrants to the U.S. Treasury Department as well as any additional capital raised from the private sector would dilute the Company s existing common shareholders.

As discussed above, if the Company is successful in raising additional capital and issues TARP preferred stock and warrants to the U.S. Treasury Department, existing common shareholders will experience significant dilution to their current ownership in the Company.

The holding company and Colonial Bank are subject to heightened regulatory scrutiny and oversight.

Due to their current condition and results of operations, BancGroup and Colonial Bank are operating under heightened regulatory scrutiny and have been and will be taking steps which are expected to improve their asset quality and capital. Colonial Bank entered into an informal Memorandum of Understanding with the FDIC and the Alabama State Banking Department on December 15, 2008, and BancGroup entered into an informal Memorandum of Understanding with the Federal Reserve Bank of Atlanta on January 6, 2009, addressing, among other items, management of asset quality and increased capital for Colonial Bank. Colonial Bank has agreed to increase its Tier I leverage ratio to 8% and its total risk-based capital ratio to 12% by March 31, 2009 and to improve asset quality by dates beginning June 30, 2009. While management is attempting to comply with these deadlines through the capital raising transactions described in Item 1 under *Executive Overview of Operations and Conditions*, failure to do so may result in the consequences described in the following paragraph. Colonial Bank may not pay dividends on its common stock owned by BancGroup without the prior written consent of the FDIC and the Alabama State Banking Department. BancGroup has agreed to use its resources to support Colonial Bank. BancGroup will not pay dividends on its common or preferred stock, purchase or redeem treasury stock, or incur additional debt or refinance existing debt without prior written consent of the Federal Reserve and the Alabama State Banking Department. Additionally, if BancGroup receives the U.S. Treasury

Department s Capital Purchase Program funds, we will be required to receive approval from the U.S. Treasury Department prior to the payment of any dividend on common stock or the repurchase of any common stock so long as any securities issued under such program remain outstanding. These matters are a major focus of the attention and efforts of the Board of Directors and management.

Failure to adequately address the regulatory concerns in these informal memoranda may result in actions by our banking regulators against BancGroup and/or Colonial Bank such as the imposition of a written agreement or a cease and desist order pursuant to Section 8 of the FDIC Act. Such actions could preclude Colonial Bank from being considered well capitalized and/or impose other restrictions or prohibitions of certain activities by BancGroup or Colonial Bank. If Colonial Bank were to be deemed an undercapitalized institution, the banking regulators could require the Bank to submit a plan for restoring Colonial Bank to an acceptable capital category, and our failure to adequately comply could eventually allow the banking regulators to appoint a receiver or conservator of Colonial Bank s net assets.

Any current or future litigation, regulatory investigations, proceedings, inquiries or changes could have a significant impact on our Company.

The financial services industry, including BancGroup, has experienced unprecedented market value declines caused primarily by the current U.S. recession and real estate market deterioration. As a result of the current market perceptions of shareholder advocacy groups as well as the new U.S. Administration in Washington, D.C., litigation, proceedings, inquiries or regulatory changes are all distinct possibilities for financial institutions. We are, and will in the future be, the subject of shareholder litigation. Such actions or changes could result in significant costs. See *Legal Proceedings* in Item 3 for more information.

The concentration of our assets in Florida makes us sensitive and more susceptible to changes in the economic, demographic and regulatory conditions in that state.

A significant portion of the loans in our portfolio are secured by residential and commercial properties in Florida. Deteriorating real estate market conditions and a significant economic downturn in Florida have negatively impacted our business. Worsening conditions in the Florida real estate markets could continue to adversely affect our borrowers ability to repay as well as impact the value of the collateral underlying our loans. Real estate values are impacted by various factors, including general economic conditions, governmental rules or policies and natural disasters. The occurrence of a natural disaster, such as a hurricane, could result in a decline in the value or destruction of mortgaged properties and an increase in the risk of delinquencies, foreclosures or loss on the uninsured portions of these loans. These factors may adversely impact our borrowers ability to make required payments, which in turn, may negatively impact our results.

Negative public opinion could damage our reputation and adversely impact our business and revenues.

As a financial institution, our earnings and capital are subject to risks associated with negative public opinion. Negative public opinion could result from our actual, alleged or perceived conduct in any number of activities, including lending practices, the failure of any product or service sold by us to meet our customers expectations or applicable regulatory requirements, corporate governance, acquisitions, as a defendant in litigation, or from actions taken by government regulators or community organizations. Negative public opinion can adversely affect our ability to attract and/or retain customers and can expose us to litigation or regulatory action. Negative public opinion could also affect our credit ratings, which are important to our access to certain sources of wholesale borrowings, thereby increasing the cost or reducing, or eliminating, the availability of these sources of funding.

Disruptions in our ability to access capital markets may negatively affect our capital resources and liquidity.

In managing our consolidated balance sheet, we depend on access to capital markets to provide us with sufficient capital resources and liquidity to meet our commitments and business needs, and to accommodate the transaction and cash management needs of our customers. Other sources of funding available to us, and upon which we rely as regular components of our liquidity risk management strategy, include deposits, inter-bank borrowings, repurchase agreements and borrowings from the Federal Home Loan Bank of Atlanta and the Federal Reserve discount window. Any occurrence that may limit our access to the capital markets, such as a decline in the confidence of depositors, debt purchasers, or counterparties participating in the capital markets, or a downgrade of our debt ratings, may adversely affect our borrowing costs and our liquidity.

Deposit pricing may continue to negatively impact our net interest margin and earnings.

Intense competition for liquidity during 2008 resulted in elevated rates being paid on time deposits, thereby compressing net interest margin and reducing net interest income. A continuation or exacerbation of such competition for time deposits would continue to adversely impact our earnings and financial condition.

Maintaining or increasing our market share depends on market acceptance and regulatory approval of new products and services.

Our success depends, in part, on our ability to adapt our products and services to evolving industry standards. There is increasing pressure on financial services companies to provide products and services at lower prices. This can reduce our net interest margin and revenues from our fee-based products and services. In addition, the widespread adoption of new technologies, including internet-based services, could require us to make substantial expenditures to modify or adapt our existing products and services. We might not successfully introduce new products and services, achieve market acceptance of our products and services and/or develop and maintain loyal customers.

The holding company relies on dividends from its subsidiaries for most of its revenue.

The holding company is a separate and distinct legal entity from its subsidiaries. It receives substantially all of its revenue from its subsidiaries. Dividends from Colonial Bank are a significant source of funds for BancGroup to pay any future dividends on the holding company s common stock. Various federal and/or state laws and regulations limit the amount of dividends that our bank and certain of our nonbank subsidiaries may pay to the holding company. Colonial Bank may not currently pay dividends on its common stock without prior written consent of its regulators. Also, the holding company s right to participate in a distribution of assets upon a subsidiary s liquidation or reorganization is subject to the prior claims of the subsidiary s creditors. For more information, refer to *Payment of Dividends and Other Restrictions* in Item 1 and Note 19, *Regulatory Matters and Restrictions.*

Our accounting policies and methods determine how we report our financial condition and results of operations, and they may require management to make estimates about matters that are inherently uncertain.

Our accounting policies and methods are fundamental to how we record and report our financial condition and results of operations. Our management must exercise judgment in selecting and applying many of these accounting policies and methods so that not only do they comply with accounting principles generally accepted in the United States but also that they reflect management s judgment as to the most appropriate manner in which to record and report our financial condition and results of operations. In some cases, management must select the accounting policy or method to apply from two or more alternatives, any of which might be reasonable under the circumstances yet might result in our reporting materially different amounts than would have been reported under a different alternative. Note 1, *Summary of Significant Accounting and Reporting Policies and Basis of Presentation*, describes our significant accounting policies.

We have identified six accounting policies as being critical to the presentation of our financial condition and results of operations because they require management to make particularly subjective and/or complex judgments about matters that are inherently uncertain and because of the likelihood that materially different amounts would be reported under different conditions or using different assumptions. These critical accounting policies relate to: (1) allowance for loan losses; (2) fair value of financial instruments; (3) purchase accounting and goodwill; (4) income taxes; (5) consolidations; and (6) stock-based compensation. A change in management s assumptions and estimates underlying these critical accounting policies could result in a material change to the Company s financial position and results of operations. For more information, refer in this report to *Critical Accounting Policies* in Management s Discussion and Analysis.

Our allowance for loan losses may not be adequate to cover actual loan losses, which may require us to take a charge to our earnings and adversely impact our financial condition and results of operations.

We maintain an allowance for estimated loan losses that we believe is adequate for absorbing the inherent losses in our loan portfolio. Management determines the provision for loan losses based upon an analysis of general market conditions, credit quality of our loan portfolio, and performance of our customers relative to their financial obligations with us. The amount of future losses is susceptible to changes in economic, operating, and other conditions, including changes in interest rates that may be beyond our control and such losses may exceed the allowance for estimated loan losses. Although management believes that the allowance for estimated loan losses is adequate to absorb any inherent losses on existing loans that may become uncollectible, there can be no assurance that the allowance will prove sufficient to cover actual loan losses in the future. Significant increases to the provision for loan losses may be necessary if material adverse changes in general economic conditions occur or the performance of our loan portfolio deteriorates. Additionally, banking regulators, as an integral part of their supervisory function, periodically review the allowance for estimated loan losses. If these regulatory agencies require us to increase the allowance for estimated loan losses, it could have a negative effect on our results of operations and financial condition.

Our financial instruments carried at fair value expose us to certain market risks.

We maintain an available for sale securities portfolio which includes various types of instruments and maturities. In addition, we elected to record selected loans held for sale at fair value. The changes in fair value of the loans held for sale that we have elected to carry at fair value are recognized in earnings. The securities and loans held for sale are exposed to market risks related to changes in interest rates, market liquidity, and market-based credit spreads, as well as to the risk of default by specific borrowers. Changes in the market values of these financial instruments could have a material adverse impact on our financial condition or results of operations. We may elect to carry additional financial assets or financial liabilities at fair value in the future.

Our mix of products and customers subjects us to potential concentration risk.

Colonial Bank offers a defined group of products, both retail and commercial, to its customers throughout the branch network. As a result of the products offered and customers served, BancGroup is subject to concentration risk. See the *Concentration* discussion within the *Risk Management* section of Management s Discussion and Analysis for further information.

We depend on the expertise of key personnel. If these individuals leave without effective replacements, operations may suffer.

The future success of our business will be dependent to a large degree on the continued services of executive officers and other key personnel who have extensive experience in the banking industry. If we lose the services of any of these integral personnel and fail to manage a smooth transition to new personnel, our business could be negatively impacted. Current compensation limits for key personnel at institutions receiving any government funds may increase the risk of loss of their services and create a competitive disadvantage with non-U.S. peer institutions or institutions not receiving any government funds.

We may not realize the expected benefits from our Colonial 1st Project.

The Colonial 1st Project, launched in December 2008, is an employee-driven effort to create a more efficient organization that delivers greater value for our shareholders and an enhanced banking experience for our customers. We are still in the early stages of this project and cannot be sure what the ultimate increase to annual pre-tax earnings will be, but other financial institutions of comparable size that have gone through this process have reported significant increases. The amounts of efficiency gains and earnings from new revenue growth initiatives are based on estimates and assumptions regarding future business performance and operating expenses. The anticipated cost savings and revenue enhancements from the Colonial 1st Project may not be achieved in their entirety or accomplished within our expected time frame. Accordingly, we cannot guarantee that the anticipated benefits from the Colonial 1st Project will be realized.

Our stock price can be volatile.

Our stock price can fluctuate widely in response to a variety of factors including, but not limited to:

- actual or anticipated variations in our quarterly operating results;
- recommendations by securities analysts;
- short selling of our stock and increased failures to deliver;
- new technology used, or services offered, by our competitors;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving us or our competitors;
- failure to integrate our acquisitions or realize anticipated benefits from our acquisitions, or, conversely, a more successful integration or realization of more benefits than anticipated;
- operating and stock price performance of other companies that investors deem comparable to us;
- news reports relating to trends, concerns and other issues in the financial services industry;
- changes in government regulations;
- geopolitical conditions such as acts or threats of terrorism or military conflicts; and
- potential actions of the banking regulators.

The current price of our common stock is below the minimum allowed by New York Stock Exchange (NYSE) listing requirements.

BancGroup s stock is listed on the NYSE. The NYSE requires that listed stocks trade at or above $1 per share. The closing price of our stock has recently fallen below $1 per share for a number of days. If the average closing price is below $1 per share for 30 consecutive trading days, the NYSE may send us a de-listing notification, which we would disclose in a press release. Within ten days after receiving such notification, we can submit a proposal to the NYSE to bring our stock price above $1 within six months. However, there can be no assurance we will be successful in implementing such a proposal. If our common stock were to be de-listed from the NYSE, it would be traded over the counter, unless we were able to list it on another exchange. A de-listing by the NYSE would likely cause trading in our stock to be less liquid.

On February 26, 2009, the NYSE announced a proposed temporary suspension of the stock-price rule through June 30, 2009. Although effective immediately, the rule is subject to a 30-day operative delay under Securities and Exchange Commission rules, for which the NYSE has requested and expects to receive a waiver. As the suspension is currently proposed, if our stock price remains below $1 per share during the suspension period, the compliance period for the 30 consecutive trading days will resume on July 1, 2009.

General market fluctuations, industry factors and general economic and political conditions and events, such as economic slowdowns or recessions, interest rate changes or credit loss trends, also could cause our stock price to decrease regardless of our operating results.

Item 1B. ***Unresolved Staff Comments***

None.

Item 2. ***Properties***

BancGroup owns its corporate offices in Montgomery, Alabama. Operations centers in Birmingham, Alabama and Orlando, Florida are leased. BancGroup maintains regional executive offices in Alabama, Florida, Georgia, Nevada and Texas.

As of December 31, 2008, Colonial Bank owned 189 and leased 158 of its full-service branches. For additional information, see Note 1, *Summary of Significant Accounting and Reporting Policies and Basis of Presentation*, Note 10, *Commitments and Contingent Liabilities*, and Note 13, *Premises and Equipment*.

Item 3. ***Legal Proceedings***

During the first quarter of 2009, BancGroup, certain officers and directors were named as defendants in purported class action lawsuits filed in the U.S. District Court for the Middle District of Alabama alleging violations of federal securities laws. These lawsuits, brought on behalf of shareholders who purchased BancGroup securities as early as January 23, 2008 and as late as January 27, 2009, allege primarily that the defendants engaged in securities fraud by disseminating materially false and misleading statements during the class period. The lawsuits seek unspecified compensatory damages (including interest), cost and expense, and injunctive relief. The lead plaintiff and class counsel have not been selected. Colonial has until March 4, 2009 to respond to the claims in the first lawsuit.

On February 24, 2009, BancGroup received notice of a shareholder derivative action filed in the Circuit Court of Montgomery County, Alabama, seeking to recover damages caused to the Company by its officers and directors. BancGroup s directors and senior officers are alleged to have breached their fiduciary obligations to the Corporation in connection with the Company s participation in the U.S. Treasury Department s TARP programs. Colonial has until March 24, 2009 to respond to the claims.

Because these lawsuits were recently filed and there are significant uncertainties involved in any potential class action litigation, management is unable to predict the outcome of the purported class action or derivative lawsuits and therefore cannot currently reasonably determine the estimated future impact on the financial condition or results of operations of the Company. BancGroup and its directors and officers intend to vigorously defend each of the lawsuits.

In the opinion of BancGroup, based on review and consultation with legal counsel, the outcome of all other litigation presently pending is not anticipated to have a material adverse effect on BancGroup s consolidated financial statements or results of operations.

Item 4. ***Submission of Matters to a Vote of Security Holders***

None.

PART II

Item 5. ***Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***

BancGroup s Common Stock is traded on the New York Stock Exchange under the symbol CNB. As of February 18, 2009, BancGroup had 202,449,152 outstanding shares of Common Stock, with 9,959 registered shareholders.

The following table indicates the high and low sales prices for and dividends paid on Common Stock during 2008 and 2007.

	Sale Price of Common Stock		Dividends Declared On Common Stock
	High	Low	(per share)
2008			
1st Quarter	**$ 16.06**	**$ 9.57**	**$ 0.190**
2nd Quarter	**10.67**	**3.38**	**0.095**
3rd Quarter	**10.50**	**3.05**	**0.095**
4th Quarter	**9.50**	**1.40**	**0.000**
2007			
1st Quarter	$ 26.80	$ 23.86	$ 0.1875
2nd Quarter	25.43	23.49	0.1875
3rd Quarter	25.50	19.30	0.1875
4th Quarter	22.47	12.85	0.1875

In the fourth quarter of 2008, BancGroup s Board of Directors suspended its quarterly dividend. The restrictions imposed upon Colonial Bank in regard to its ability to pay dividends to BancGroup, which in turn limit BancGroup s ability to pay dividends, are described further herein as well as in *Payment of Dividends and Other Restrictions* in Item 1.

The information required by this item concerning Equity Compensation Plans is included in Item 12 and Note 22, *Stock-Based Compensation*, both of which are incorporated herein by reference.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs(1)
Cumulative through December 31, 2007	8,606,800	$ 24.26	8,606,800	$ 91,175,000
January 1 December 31, 2008		$		$ 91,175,000
Cumulative through December 31,2008	8,606,800	$ 24.26	8,606,800	$ 91,175,000

(1) Information is as of the end of the period.

In 2006, the Company publicly announced two share repurchase programs to purchase shares of BancGroup Common Stock not to exceed a combined total of $150 million. During 2007, both of these repurchase programs were completed. On June 11, 2007, the Company publicly announced another share repurchase program to purchase shares of BancGroup Common Stock not to exceed $150 million, of which approximately $91.2 million has yet to be purchased. This program will terminate on the earlier of its completion or June 8, 2009. BancGroup did not make any purchases during 2008 and is not expected to make any purchases in 2009.

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Shareholder Performance Graph

Set forth below is a line graph comparing the five-year cumulative return of BancGroup common stock, based on an initial investment of $100 on December 31, 2003 and assuming reinvestment of dividends, with that of the Standard & Poor s 500 Index (the S&P 500) and the S&P 500 Bank Index and the KBW Regional Banks index. The comparisons in this graph are set forth in response to the Securities and Exchange Commission s (the SEC) disclosure requirements, and therefore are not intended to forecast or be indicative of future performance of the common stock.

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Item 6. ***Selected Financial Data***

The following table sets forth selected financial data for the last five years:

	2008	2007	2006	2005	2004
		(In thousands, except per share amounts)			
Statement of Income:					
Interest income	**$ 1,385,827**	$ 1,556,485	$ 1,455,585	$ 1,162,055	$ 848,017
Interest expense	**722,314**	795,111	700,318	452,833	280,769
Net interest income	**663,513**	761,374	755,267	709,222	567,248
Provision for loan losses	**728,942**	106,450	22,142	26,838	26,994
Net interest income after provision for loan losses	**(65,429)**	654,924	733,125	682,384	540,254
Noninterest income	**203,896**	186,224	189,222	175,976	153,201
Noninterest expense excluding goodwill impairment	**670,262**	559,678	519,601	515,255	431,649
Goodwill impairment	**575,000**				
Minority interest expense/REIT preferred dividends	**21,344**	12,984			
Income (loss) before income taxes	**(1,128,139)**	268,486	402,746	343,105	261,806
Income tax expense (benefit)	**(247,667)**	87,561	136,933	114,603	88,929
Net Income (Loss)	**$ (880,472)**	$ 180,925	$ 265,813	$ 228,502	$ 172,877
Earnings (loss) Per Common Share:					
Net income (loss):					
Basic	**$ (4.71)**	$ 1.18	$ 1.73	$ 1.53	$ 1.32
Diluted	**(4.71)**	1.17	1.72	1.52	1.31
Average shares outstanding:					
Basic	**186,897**	153,519	153,598	149,053	131,144
Diluted	**186,897**	154,391	154,810	150,790	132,315
Cash dividends per common share	**$ 0.38**	$ 0.75	$ 0.68	$ 0.61	$ 0.58

	2008	2007	2006	2005	2004
			(In thousands)		
Statement of Condition data at year end:					
Total assets	**$ 25,816,306**	$ 25,975,989	$ 22,784,249	$ 21,426,197	$ 18,896,610
Interest bearing deposits in banks and the Federal Reserve	**1,534,463**	28,993	2,200	9,417	3,828
Securities purchased under agreements to resell	**1,556,157**	2,049,664	605,937	589,902	221,491
Total securities	**3,503,380**	3,682,510	3,085,488	2,844,354	3,653,554
Loans, net of unearned income	**14,530,018**	15,923,178	15,478,889	14,899,864	12,857,811
Loans held for sale	**2,082,248**	1,544,222	1,474,000	1,097,892	678,496
Non-time deposits	**7,989,907**	9,771,573	9,092,663	9,012,943	7,546,038
Total deposits	**18,673,265**	18,544,267	16,091,054	15,483,449	11,863,695
Long-term debt	**4,043,807**	4,023,836	2,522,273	2,338,831	2,260,957
Shareholders equity	**1,344,978**	2,273,571	2,057,335	1,932,691	1,398,291
Average balances:					
Total assets	**26,761,999**	23,845,264	22,237,690	20,682,310	17,433,571
Interest-earning assets	**24,308,648**	21,636,867	20,409,906	18,943,511	16,173,539
Interest bearing deposits in banks and the Federal Reserve	**334,294**	10,504	3,887	23,748	7,734
Securities purchased under agreements to resell	**2,029,631**	1,467,233	592,840	489,688	76,554
Total securities	**3,811,537**	3,170,823	3,014,453	3,400,782	3,397,000
Loans, net of unearned income	**15,454,146**	15,290,766	15,339,699	14,139,380	12,148,513
Loans held for sale	**2,598,804**	1,613,170	1,374,115	823,177	497,315

Non-time deposits	**8,830,863**	9,278,950	9,080,151	8,543,542	6,847,334
Total deposits	**18,685,112**	16,566,120	15,788,319	13,987,525	10,862,040
Shareholders equity	**2,264,692**	2,166,296	1,992,772	1,779,081	1,285,772

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	2008	2007	2006	2005	2004
Selected Financial Measures:					
Net income to:					
Average assets	**NM**	0.76%	1.20%	1.10%	0.99%
Average shareholders equity	**NM**	8.35	13.34	12.84	13.45
Noninterest income/average assets	**0.76%**	0.78	0.85	0.85	0.88
Noninterest expense/average assets	**4.65**	2.35	2.34	2.49	2.48
Efficiency ratio[(1)]	**142.17**	58.68	54.94	58.11	59.76
Dividend payout ratio	**NM**	64.10	39.53	40.13	44.27
Shareholders equity to assets	**5.21**	8.75	9.03	9.02	7.40
Tangible common equity ratio	**3.41**	4.83	6.26	5.97	5.43
Tangible capital ratio	**4.56**	6.00	6.26	5.97	5.43
Book value per share	**$ 6.64**	$ 14.44	$ 13.46	$ 12.53	$ 10.45
Tangible book value per share	**$ 4.26**	$ 7.63	$ 9.05	$ 8.02	$ 7.50
Risk-based capital:[(2)]					
Tier I	**8.58%**	8.22%	9.09%	9.15%	8.80%
Total	**12.88**	11.01	11.77	12.17	11.39
Tier I leverage[(2)]	**5.90**	6.67	7.81	7.77	7.16
Total nonperforming assets to net loans, other real estate and repossessions[(3)]	**4.83**	0.86	0.16	0.21	0.29
Net charge-offs to average loans	**4.16**	0.35	0.12	0.14	0.19
Allowance for loan losses to total loans (net of unearned income)	**2.24**	1.50	1.13	1.15	1.16
Allowance for loan losses to nonperforming loans[(3)]	**61**	196	1247	662	548
Non-GAAP Measures:[(4)]					
Core noninterest income/average assets[(5)]	**0.75**	0.88	0.82	0.85	0.84
Core noninterest expense/average assets[(6)]	**2.46**	2.27	2.33	2.42	2.42
Core efficiency ratio[(7)]	**75.52**	55.49	55.34	56.58	59.04

(1) Includes a goodwill impairment charge of $575.0 million for 2008. Refer to Note 14, *Goodwill and Other Intangible Assets*, in the Notes to Consolidated Financial Statements for additional information.

(2) Refer to Note 19, *Regulatory Matters and Restrictions,* in the Notes to Consolidated Financial Statements for additional information.

(3) Nonperforming loans and nonperforming assets are shown as defined in the *Risk Management* section of Management s Discussion and Analysis.

(4) Management believes that these non-GAAP measures provide information that is useful to investors in understanding the performance of the Company s underlying operations and performance trends. Specifically, these measures permit evaluation and comparison of results for ongoing business operations, and it is on this basis that Management internally assesses the Company s performance.

(5) Excluded from core noninterest income are securities and derivatives gains (losses), net totaling $3.0 million, $4.0 million, $4.8 million, ($24.7) million, and $7.5 million for 2008, 2007, 2006, 2005, and 2004, respectively; securities restructuring charges of ($36.0) million for 2007; gain on sale of mortgages and businesses of $8.8 million and $2.8 million for 2007 and 2006, respectively; gain on sale of branches of $37.0 million for 2005; and changes in fair value of swap derivatives of ($12.1) million for 2005 and ($0.4) million for 2004.

(6) Excluded from core noninterest expense are severance expense of $786,000, $6.6 million and $413,000 for 2008, 2007 and 2006, respectively; merger related expenses of $4.0 million, $4.2 million, and $2.0 million for 2007, 2005, and 2004, respectively; net losses related to the early extinguishment of debt of $10.3 million, $6.9 million, $9.6 million and $7.4 million for 2008, 2007, 2005 and 2004, respectively; and goodwill impairment of $575.0 million for 2008.

(7) This ratio utilizes core noninterest income and core noninterest expense as detailed in notes (5) and (6) above.

NM Not meaningful

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Selected Quarterly Financial Data 2008-2007

	2008				2007			
	Dec. 31	Sept. 30	June 30	March 31	Dec. 31	Sept. 30	June 30	March 31
	(In thousands, except per share amounts)							
Interest income	**$ 318,133**	**$ 336,417**	**$ 347,740**	**$ 383,537**	$ 400,197	$ 395,534	$ 383,874	$ 376,880
Interest expense	**177,417**	**169,668**	**173,316**	**201,913**	204,996	199,523	193,657	196,935
Net interest income	**140,716**	**166,749**	**174,424**	**181,624**	195,201	196,011	190,217	179,945
Provision for loan losses	**455,000**	**159,399**	**79,000**	**35,543**	93,295	4,800	6,105	2,250
Net interest income after provision for loan losses	**(314,284)**	**7,350**	**95,424**	**146,081**	101,906	191,211	184,112	177,695
Noninterest income	**44,786**	**45,640**	**55,723**	**57,747**	59,266	52,958	58,781	15,219
Noninterest expense excluding goodwill impairment	**179,680**	**162,439**	**164,167**	**163,978**	145,102	134,951	141,484	138,141
Goodwill impairment	**575,000**							
Minority interest expense/REIT preferred dividends	**5,336**	**5,336**	**5,336**	**5,336**	5,336	5,336	2,312	
Income tax expense (benefit)	**(204,409)**	**(43,575)**	**(9,400)**	**9,717**	1,762	34,527	32,978	18,294
Net income (loss)	**$ (825,105)**	**$ (71,210)**	**$ (8,956)**	**$ 24,797**	$ 8,972	$ 69,355	$ 66,119	$ 36,479
Earnings (Loss) Per Share:								
Net income (loss)								
Basic	**$ (4.11)**	**$ (0.35)**	**$ (0.05)**	**$ 0.16**	$ 0.06	$ 0.45	$ 0.43	$ 0.24
Diluted	**$ (4.11)**	**$ (0.35)**	**$ (0.05)**	**$ 0.16**	$ 0.06	$ 0.45	$ 0.43	$ 0.24

Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

This annual report to shareholders, the Annual Report on Form 10-K and the information incorporated by reference contain forward-looking statements within the meaning of the federal securities laws. Words such as believes , estimates , plans , expects , should , may , might , could , outlook , potential , would , anticipates , the negative of these terms and similar expressions as they relate to BancGroup (including its subsidiaries and its management), are intended to identify forward-looking statements. The forward-looking statements in these reports are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in or implied by the statements.

In addition to factors mentioned elsewhere in this annual report or previously disclosed in BancGroup s SEC reports (accessible on the SEC s website at www.sec.gov or on BancGroup s website at www.colonialbank.com), the following factors, among others, could cause actual results to differ materially from forward-looking statements, and future results could differ materially from historical performance. These factors are not exclusive:

losses in our loan portfolio are greater than estimated or expected;

an inability to raise additional capital on terms and conditions that are satisfactory;

failure to receive final approval for the U.S. Treasury Department s Capital Purchase Program;

the impact of current economic conditions and the impact of our results of operations on our ability to borrow additional funds to meet our liquidity needs;

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economic conditions affecting real estate values and transactions in BancGroup s market and/or general economic conditions, either nationally or regionally, that are less favorable or take longer to recover than expected;

changes in the interest rate environment which expand or reduce margins or adversely affect critical estimates as applied and projected returns on investments and fair values of assets;

continued or sustained deterioration of market and economic conditions or business performance could increase the likelihood that we would have an additional goodwill impairment charge;

deposit attrition, customer loss or revenue loss in the ordinary course of business;

increases in competitive pressure in the banking industry and from non-banks;

costs or difficulties related to the integration of the businesses of BancGroup and institutions it acquires are greater than expected;

the inability of BancGroup to realize elements of its strategic and operating plans for 2009 and beyond;

natural disasters in BancGroup s primary market areas result in prolonged business disruption or materially impair the value of collateral securing loans;

management s assumptions and estimates underlying critical accounting policies prove to be inadequate or materially incorrect or are not borne out by subsequent events;

the impact of recent and future federal and state regulatory changes;

current or future litigation, regulatory investigations, proceedings or inquiries;

strategies to manage interest rate risk may yield results other than those anticipated;

changes which may occur in the regulatory environment;

a significant rate of inflation (deflation);

unanticipated litigation or claims;

changes in the securities markets;

- *acts of terrorism or war; and*

- *details of the recently enacted Emergency Economic Stabilization Act of 2008, the American Recovery and Reinvestment Act of 2009 and various announced and unannounced programs implemented by the U.S. Treasury Department and bank regulators to address capital and liquidity concerns in the banking system, are still being finalized and may have a significant effect on the financial services industry and BancGroup.*

Many of these factors are beyond BancGroup s control. The reader is cautioned not to place undue reliance on any forward looking statements made by or on behalf of BancGroup. Any such statement speaks only as of the date the statement was made or as of such date that may be referenced within the statement. BancGroup does not undertake any obligation to update or revise any forward-looking statements.

Management s Discussion and Analysis of Financial Condition and Results of Operations is presented on the following pages. The principal purpose of this review is to provide the reader of the attached financial statements and accompanying notes with a detailed analysis of the financial results of The Colonial BancGroup, Inc. and subsidiaries.

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EXECUTIVE OVERVIEW

The Colonial BancGroup, Inc. is a $25.8 billion financial services company providing diversified services including retail and commercial banking, wealth management services, mortgage banking and insurance products through its branch network, private banking offices or officers, ATMs and the internet as well as other distribution channels to consumers and businesses. At December 31, 2008, BancGroup had 347 branches in Florida, Alabama, Georgia, Nevada and Texas.

The following chart includes the Company s assets, deposits and branches by state as of December 31, 2008.

	Assets		Deposits		Branches	
	Amount	%	Amount	%	Number	%
			(Dollars in millions)			
Florida	$ 15,949	62%	$ 10,770	58%	197	57%
Alabama	4,422	17%	4,224	23%	90	26%
Georgia	1,286	5%	775	4%	19	5%
Texas	1,778	7%	793	4%	21	6%
Nevada	976	4%	833	4%	20	6%
Corporate/Other	1,405	5%	1,278	7%		
Total	$ 25,816	100%	$ 18,673	100%	347	100%

Strategy

BancGroup is built upon the foundation of a community banking philosophy that emphasizes local responsibility for customer relationships. The local market personnel are supported by centralized operations, which allow the local banking officers to concentrate on serving their customers. Through this structure of local customer relationship responsibility and centralized operations, the local banking officers generally have customer level decision making capability while at the same time having an operational support structure.

Overview of Financial Condition and Earnings

Earnings

Colonial incurred a net loss for the year ended December 31, 2008 of $4.71 per diluted share, a significant decrease from the $1.17 earned in 2007. Colonial s net loss for the year was $880 million compared to net income of $181 million for 2007. The 2008 loss was driven by credit costs and goodwill impairment which are more fully described below.

Colonial s net interest income decreased 13% from 2007, driven by a 79 basis point compression of net interest margin. The net interest margin for 2008 was 2.76% compared to 3.55% for 2007. The margin compression was driven by these primary factors: (1) a 35 basis point reduction from the impact of customer preference for certificates of deposits, which resulted in a mix change to higher cost deposits from low cost deposits and fierce deposit pricing competition during 2008 which kept deposit rates high compared to other market rates; (2) a 20 basis point reduction from the impact of credit related reductions on interest income, including interest reversals when loans are placed on nonaccrual status as well as a lack of income while those loans remain on nonaccrual status and (3) a 16 basis point reduction from a decrease in loans which were replaced with lower yielding assets. These factors caused yields on interest earning assets to contract by 148 basis points while the cost of deposits only decreased 69 basis points despite a decrease of 296 basis points in the average Federal Funds rate.

Noninterest income for 2008 increased 9% from 2007. Mortgage warehouse fees decreased by $17.0 million as a result of discontinuing the sales of assets to the commercial paper conduits in January 2008. Other income also declined by $6.2 million due to less income from joint ventures and gains on the sales of assets. These decreases were partially offset by increases in mortgage banking origination and sales of $15.0 million and wealth management revenues of $1.2 million. Non-core items increased over 2007 by $26.3 million, primarily due to the securities restructuring charges of $36.0 million recognized in 2007.

Noninterest expense increased in 2008 by 122%, or $685.6 million, compared to 2007. The increase reflects a noncash goodwill impairment charge of $575.0 million in 2008, increased losses and expenses on other real estate of $27.2 million, increased losses on equity investments of $13.9 million, increased FDIC insurance and other regulatory fees of $11.8 million as 2007 fees were substantially offset by credits, increased costs related to the addition of branches through acquisition and de novo expansion and a net loss on early extinguishment of debt totaling $10.3 million. Reductions in severance expense and merger related expenses of $5.8 million and $4.0 million, respectively, partially offset the increases.

Colonial recorded a noncash charge of $575.0 million in the fourth quarter of 2008 for goodwill impairment. Goodwill recorded on past acquisitions in Florida and Nevada became impaired in the fourth quarter primarily due to declining bank market valuations and increased credit costs. Refer to the *Goodwill* section of Management s Discussion and Analysis for additional information.

Colonial s loan loss provision was $728.9 million in 2008 compared to $106.5 million in 2007. The Company provided for net charge-offs of $642.8 million in 2008 and increased its allowance for loan losses by $86.2 million to $325.0 million, or 2.24% of net loans, at December 31, 2008 compared to $238.8 million, or 1.50% of net loans, at December 31, 2007.

Asset Quality

For the year ended December 31, 2008, Colonial charged off $642.8 million of loans compared to $54.1 million for 2007, and recorded provision for loan losses of $728.9 million, compared to $106.5 million for 2007. With provision exceeding net charge-offs, the allowance for loan losses increased to 2.24% of net loans at December 31, 2008, from 1.50% at December 31, 2007. Nonperforming assets were $710.5 million, or 4.83%, of loans, net of unearned income, and other real estate, at December 31, 2008, compared to $137.6 million, or 0.86%, at December 31, 2007. At December 31, 2008, 79% of Colonial s nonperforming assets were real estate construction-related. During 2008, Colonial reduced real estate construction loans to $4.9 billion, a $1.4 billion, or 22%, reduction compared to December 31, 2007.

Liquidity

The Company s liquidity position at December 31, 2008 exceeded the Company s forecasted cash uses for 2009.

The Company s primary source of funding is deposits which funded 72% of total assets at December 31, 2008. During 2008, deposits increased $129.0 million to $18.7 billion, with retail deposits comprising $17.4 billion of the total. Colonial has chosen to participate in the deposit insurance component of the Temporary Liquidity Guarantee Program (TLGP) and as such, the FDIC insures up to $250,000 per deposit relationship and provides unlimited deposit insurance for certain transaction accounts. All banks that participate in the TLGP deposit insurance program have the same FDIC insurance coverage. Time deposits of $9.4 billion that mature during 2009 are expected to be renewed or substantially replaced by new originations. Total deposits increased after year end to $19.5 billion on February 28, 2009.

During 2009, only $42.4 million of the Company s long-term debt will mature. The Company expects to repay the debt as it becomes due.

In response to the significant market and economic uncertainty in the United Sates, Colonial had cash and interest bearing deposits in banks and the Federal Reserve of over $2.0 billion at December 31, 2008.

Capital

BancGroup s total risk-based capital ratio at December 31, 2008 was 12.88%, and its Tier I risk-based capital ratio was 8.58%, exceeding the regulatory definitional guidelines for well capitalized of 10% and 6%, respectively. The Company s total and Tier I risk-based capital ratios at December 31, 2007 were 11.01% and 8.22%, respectively. The Company s Tier I leverage ratios were 5.90% and 6.67% at December 31, 2008 and 2007, respectively, also exceeding the regulatory guidelines for well capitalized of 5%.

Dividends

In 2008, the Company paid dividends of $68.4 million, or $0.38 per share to its shareholders, compared to $115.0 million, or $0.75 per share, in 2007. The Company suspended dividend payments in the fourth quarter of 2008.

Business Combinations

While Colonial did not make any acquisitions during 2008, the Company made two acquisitions in 2007 Miami, Florida based Commercial Bankshares, Inc. and its subsidiary Commercial Bank of Florida, and Lakeland, Florida based Citrus & Chemical Bancorporation, Inc. and its subsidiary Citrus & Chemical Bank. For more information about the 2007 acquisitions, refer to Note 4, *Business Combinations*, in the Notes to Consolidated Financial Statements.

CRITICAL ACCOUNTING POLICIES

BancGroup s significant accounting and reporting policies are presented in Note 1, *Summary of Significant Accounting and Reporting Policies and Basis of Presentation*. These policies, along with the disclosures presented in the other notes, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Those accounting policies involving significant estimates and assumptions by management, which have, or could have, a material impact on the carrying value of certain assets and impact comprehensive income, are considered critical accounting policies. BancGroup recognizes the following as critical accounting policies: Allowance for Loan Losses, Fair Value of Financial Instruments, Purchase Accounting and Goodwill, Income Taxes, Consolidations and Stock-Based Compensation.

Allowance for Loan Losses

Management s ongoing evaluation of the adequacy of the allowance considers both impaired and unimpaired loans and takes into consideration the Company s past loan loss experience, known and inherent risks in the portfolio, existing adverse situations that may affect the borrowers ability to repay, estimated value of any underlying collateral, an analysis of existing guarantees and an analysis of current economic conditions. While management believes that it has exercised prudent judgment and applied reasonable assumptions which have resulted in an allowance presented in accordance with generally accepted accounting principles, there can be no assurance that in the future, adverse economic conditions, increased nonperforming loans or other factors will not require further increases in the allowance. A more detailed discussion of BancGroup s allowance for loan losses is included in the *Risk Management* section of Management s Discussion and Analysis as well as Note 1, *Summary of Significant Accounting and Reporting Policies and Basis of Presentation*.

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The table below illustrates BancGroup s sensitivity to changes in certain factors used in the determination of the allowance for loan losses.

Factors	Estimated Effect on 2008 Provision Expense Assuming the Following Changes in Each Determining Factor[2] +10%	-10%
	(In thousands)	
Loan portfolio size	$ 25,160	$ (25,160)
Net charge-offs	20,625	(20,625)
Criticized loans[1]	9,107	(9,107)

(1) Criticized loans include all loans rated special mention or worse.
(2) These computations do not contemplate any action BancGroup could or would undertake in response to changes in each of these risk factors.

Fair Value of Financial Instruments

A portion of BancGroup s assets and liabilities are measured at fair value on a recurring basis, including securities available for sale, loans held for sale for which BancGroup has elected the fair value option, and derivative assets and liabilities. Certain other assets are measured at fair value on a nonrecurring basis. These adjustments to fair value usually result from application of lower of cost or fair value accounting or write-downs of individual assets due to impairment. Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards (SFAS) 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value, and expands disclosures about assets and liabilities measured at fair value. SFAS 157 defines fair value as the price that would be received to sell a financial asset or to transfer a financial liability in an orderly transaction between market participants at the measurement date. SFAS 157 establishes a three-level hierarchy for disclosure of assets and liabilities recorded at fair value. This classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used in the measurement are observable or unobservable. Observable inputs reflect market-driven or market-based information obtained from independent sources, while unobservable inputs reflect the Company s estimates about market data. These three levels of inputs that may be used to measure fair value are:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Directly or indirectly observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability (for example, interest rates and yield curves observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks, and default rates); or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities would include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

In accordance with SFAS 157, it is the Company s policy to maximize the use of observable inputs and to minimize the use of unobservable inputs when developing fair value measurements. When active markets exist, quoted market prices for identical or similar financial instruments are used to measure fair value. In the absence of active markets, management determines the fair value of BancGroup s assets and liabilities using models which are based on management s judgment, assumptions and estimates regarding credit quality, liquidity,

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interest rates and other relevant inputs. A substantial portion of the Company s financial instruments are measured using Level 1 or Level 2 inputs. However, in certain cases, when market observable prices and inputs are not based on actively traded instruments, judgments must be made about assumptions market participants would use in estimating the fair value of the financial instrument.

The degree of judgment involved in determining the fair value of a financial instrument depends on the availability of quoted market prices or observable market data from active markets. For financial instruments that trade actively and have quoted market prices or observable market data, there is minimal subjectivity. When observable market data from active markets is not available, judgment is necessary to estimate fair value. In addition, changes in market conditions may reduce the availability of quoted market prices or observable market data. For example, reduced liquidity in the capital markets or changes in secondary market activity could result in observable market data becoming unavailable. Therefore, when market data is not available, the Company uses valuation methods requiring more management judgment to estimate fair value.

Carrying financial assets and liabilities at fair value inherently results in more financial statement volatility as compared to carrying such assets and liabilities at historical or amortized cost. At December 31, 2008, $5.1 billion, or 19.6%, of BancGroup s total assets were measured at fair value on a recurring basis. Approximately 76.2% of these assets were classified as Level 1 or Level 2 within the fair value hierarchy. At December 31, 2008, $27.3 million, or 0.1%, of BancGroup s total liabilities were measured at fair value on a recurring basis. Approximately 1.5% of these liabilities were classified as Level 1 or Level 2 within the fair value hierarchy. The measurement of these financial instruments therefore is less subjective to judgment than those classified as Level 3 as they are based upon quoted market prices or observable market-driven or market-based information.

At December 31, 2008, $378.5 million, or 1.5%, of BancGroup s total assets were measured at fair value on a nonrecurring basis. Approximately 1.9% of these assets were classified as Level 1 or Level 2. At December 31, 2008, there were no liabilities measured at fair value on a nonrecurring basis.

Level 3 assets measured at fair value on a recurring basis were 23.8% of total assets measured at fair value and 4.7% of total assets at December 31, 2008. Level 3 liabilities measured at fair value on a recurring basis were 98.5% of total liabilities measured at fair value and 0.1% of total liabilities at December 31, 2008.

Level 3 assets and liabilities measured at fair value on a recurring basis as of December 31, 2008 include the following: the Company s call options related to interests in short-term participations in mortgage loans, interest rate lock commitments and the related forward sales commitments which were transferred into Level 3 during the second quarter of 2008 due to the significance of unobservable inputs (such as the probability of funding) to the overall value of these instruments; and, the Company s non-agency mortgage-backed securities which were transferred into Level 3 in the third quarter of 2008. The transfer of these securities available for sale into Level 3 was based on a significant reduction in market liquidity for these securities. In valuing Level 3 assets and liabilities, significant inputs include market interest rates, future cash flows, the fair value of underlying mortgages (call options, interest rate lock commitments and forward sales commitments) and pull through rates (interest rate lock commitments and forward sales commitments). For further discussion on Level 3 instruments, see Note 5, *Fair Value Measurements.*

Imprecision in estimating unobservable market inputs can impact the amount of income or loss recorded for a particular fair value measurement. Furthermore, while BancGroup believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. For a detailed discussion of the determination of fair value for individual financial instruments, see Note 5, *Fair Value Measurements.*

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Purchase Accounting and Goodwill

For an acquisition, BancGroup is generally required to record the assets acquired, including identified intangible assets, and liabilities assumed at their fair value, which often involves estimates based on third-party valuations, such as appraisals, or internal valuations based on discounted cash flow analyses or other valuation techniques, which are inherently subjective. The amortization of identifiable intangible assets is based upon the estimated economic benefits to be received, which is also subjective. These estimates also include the establishment of various accruals and allowances based on planned facility dispositions and employee severance considerations, as well as other acquisition-related items.

BancGroup records goodwill in an amount equal to the excess of the cost of an acquisition over the fair value of the net assets acquired. BancGroup tests goodwill for impairment on an annual basis, or more often if events or circumstances indicate that there may be impairment. The Company has elected to perform its annual testing as of September 30 each year. The goodwill impairment test is a two-step process, which requires management to make judgments in determining the assumptions used in the calculations. The first step involves estimating the fair value of each reporting unit and comparing it to the reporting unit s carrying value, which includes the allocated goodwill. If the estimated fair value is less than the carrying value, then a second step is performed to measure the actual amount of goodwill impairment. The second step initially involves determining the implied fair value of goodwill. This requires the Company to allocate the estimated fair value to all the assets and liabilities of the reporting unit. Any unallocated fair value represents the implied fair value of goodwill which is compared to its corresponding carrying value. If the implied fair value is less than the carrying value, an impairment loss is recognized in an amount equal to that deficit.

Fair values of reporting units are estimated using discounted cash flow models derived from internal earnings forecasts. The key assumptions used to estimate the fair value of each reporting unit include earnings forecasts for five years, terminal values based on estimated future growth rates and discount rates that reflect the range of the Company s market capitalization plus a control premium.

The more significant fair value adjustments in the second step of the impairment test were to loans in each of the reporting units. These adjustments reflect current market conditions and include significant liquidity discounts. Also, the step two analysis included adjustments to previously recorded identifiable intangible assets to reflect them at fair value and also included the fair value of additional intangibles not previously recognized. The adjustments to measure the assets, liabilities and intangibles at fair value are for the purpose of measuring the implied fair value of goodwill and such adjustments are not reflected in the Consolidated Statements of Condition.

The Company s annual goodwill impairment test was performed as of September 30, 2008. As a result of the annual impairment test, even though four reporting units were required to perform a second step analysis, management determined that no goodwill impairment charge was required at that time, as the implied fair value of goodwill for each tested reporting unit exceeded its carrying value. Due to the decline in market valuations for financial institutions, including Colonial, and an increase in credit costs during the fourth quarter of 2008, an interim impairment test was performed as of December 31, 2008. As a result of the interim impairment test, the Company computed and recorded a $575.0 million goodwill impairment loss in the fourth quarter of 2008, reducing the balance of goodwill to the implied fair value from the second step of the impairment test. See Note 14, *Goodwill and Other Intangible Assets,* for additional information.

Due to the ongoing uncertainty in market conditions, which may continue to negatively impact the performance of BancGroup s reporting units as well as the market valuations of financial institutions, including Colonial, management will continue to monitor and evaluate the carrying value of goodwill. Additional goodwill impairment could be recorded in future periods and such impairment could be material to the Company s results of operations.

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The table below illustrates BancGroup s sensitivity to changes in the rates used in discounting the estimated future cash flows. The sensitivity analysis was based on information available as of the interim test date of December 31, 2008. Further discussion regarding BancGroup s accounting for goodwill is included at Note 1, *Summary of Significant Accounting and Reporting Policies and Basis of Presentation.*

	Sensitivity of Goodwill Impairment Analysis Results Assuming the Following Changes in Discount Rates(1)		
	No Change	+10%	- 10%
		(In thousands)	
Total goodwill impairment	$ 575,000	$ 676,970	$ 416,365

(1) These computations do not take into account changes in the forecasted cash flows and future annual growth rates. Further, the computations do not contemplate any action BancGroup could undertake in response to changes in the risks associated with the operations of each reporting unit.

Income Taxes

BancGroup uses the asset and liability method of accounting for income taxes. Determination of the deferred and current provision requires analysis by management of certain transactions and the related tax laws and regulations. Management exercises significant judgment in evaluating the amount and timing of recognition of the resulting tax liabilities and assets. Those judgments and estimates are re-evaluated on a continual basis as regulatory and business factors change.

The Company periodically reviews the carrying amount of its deferred tax assets to determine if the establishment of a valuation allowance is necessary. If, based on the available evidence in future periods, it is more likely than not that all or a portion of the Company s deferred tax assets will not be realized, a deferred tax valuation allowance would be established and could be material to the results of operations. Consideration is given to all positive and negative evidence related to the realization of the deferred tax assets.

In evaluating the available evidence, management considers historical financial performance, expectation of future earnings, the ability to carryback losses to recoup taxes previously paid, length of statutory carryforward periods, experience with operating loss and tax credit carryforwards not expiring unused, tax planning strategies and timing of reversals of temporary differences. Significant judgment is required in assessing future earnings trends and the timing of reversals of temporary differences. The Company s evaluation is based on current tax laws as well as management s expectations of future performance based on its strategic initiatives. Changes in existing tax laws and future results that differ from expectations may result in significant changes in the deferred tax asset valuation allowance. See Note 25, *Income Taxes,* for additional information.

Effective January 1, 2007, the Company adopted Financial Accounting Standards Board (FASB) Interpretation (FIN) 48, *Accounting for Uncertainty in Income Taxes*, which establishes a two-step process for recognizing and measuring tax benefits. FIN 48 applies to all tax positions within the scope of SFAS 109, *Accounting for Income Taxes*. Under FIN 48, tax benefits can only be recognized in BancGroup s financial statements if it is more likely than not that the benefits would be sustained after full review by the relevant taxing authority.

The application of income tax law is inherently complex. Laws and regulations in this area are voluminous, are often ambiguous and are frequently amended. Colonial is required to make many subjective assumptions and judgments regarding income tax exposures. Interpretations of and guidance surrounding income tax laws and regulations change over time. As such, changes in the Company s subjective assumptions and judgments can materially affect amounts recognized in the consolidated balance sheets and statements of income.

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Consolidations

The Company enters into a variety of financing and investing arrangements in the normal course of business. Financing arrangements are entered into to meet balance sheet management, funding, liquidity and market or credit risk management needs. Investing arrangements are entered into in order to earn a return on investment. Because certain financing arrangements are made through legal entities and certain investments are in separate legal entities, the Company must evaluate whether or not these entities should be consolidated into the Company for financial reporting. In determining whether the entities involved in these arrangements should be consolidated, the Company first considers the guidance in Accounting Research Bulletin 51, *Consolidated Financial Statements,* which requires a company s consolidated financial statements to include subsidiaries in which the company has a controlling financial interest. This requirement is usually applied to subsidiaries in which a company has a majority voting interest. However, for entities that are not controllable through voting interests or in which the equity investors do not bear the residual economic risks, the Company follows the guidance in FIN 46(R), *Consolidation of Variable Interest Entities*. Determining whether a variable interest entity (VIE) should be consolidated requires the Company to make estimates about the VIE s expected losses and expected residual returns, as well as the extent to which those expected losses and expected residual returns will be absorbed by the Company. If the Company absorbs a majority of either, it is considered the primary beneficiary and is required to consolidate the VIE.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted SFAS 123(R), *Share-Based Payment,* which requires all stock-based payments to employees to be recognized in the income statement based on their fair values. Prior to January 1, 2006, the Company accounted for stock based-compensation under the intrinsic value method prescribed by Accounting Principles Board (APB) Opinion 25, which only required the recognition of compensation cost for the excess, if any, of the quoted market price of the stock at the grant date or other measurement date over the amount an employee must pay to acquire the stock. As such, under APB 25 the Company generally recognized no compensation expense for stock options since the exercise prices equaled the market prices of BancGroup common stock on the grant dates. The Company did, however, recognize compensation cost for restricted stock awards since such awards have no exercise price. Also, under APB 25 the Company accounted for forfeitures as they occurred. Under SFAS 123(R), the Company is required to estimate forfeitures for awards which are not expected to vest.

The Company adopted SFAS 123(R) using the modified prospective transition method which did not require the restatement of prior periods to reflect the fair value method of expensing stock-based compensation. SFAS 123(R) did require a cumulative effect adjustment of previously recognized compensation expense in order to estimate forfeitures for awards outstanding on the adoption date. The cumulative effect adjustment was immaterial.

The Company estimates the fair value of stock options using the Black-Scholes valuation model, which requires the input of subjective assumptions including expected option term and expected stock price volatility. Further, the Company now estimates forfeitures for awards granted which are not expected to vest. Changes in these assumptions and estimates can materially affect the calculated fair value of stock-based compensation and the related expense to be recognized. As a result of implementing SFAS 123(R), the Company refined its process for estimating option term and expected stock price volatility.

For options granted during 2008, 2007 and 2006, the expected option term was determined based upon analysis of the Company s historical experience with exercise and post-vesting termination behavior of employees. The resulting expected option term was 5.33 years. The expected volatility was determined based upon historical daily prices of the Company s common stock over the most recent period equal to the expected option term, as well as implied price volatility based on the Company s exchange traded options. The indicated historical and implied volatilities were weighted 75% and 25%, respectively. Less emphasis was placed on implied volatility compared to historical volatility because the volume of exchange traded options is relatively low. The resulting weighted average expected volatility was 34.9%, 21.4% and 22.8% in 2008, 2007 and 2006, respectively. The expected forfeiture rate was determined based on analysis of the Company s historical experience with employees pre-vesting termination behavior.

As of December 31, 2008, the total unrecognized compensation cost related to nonvested awards was $11.8 million. The unrecognized compensation cost is expected to be recognized over a weighted average period of 3.1 years.

REVIEW OF RESULTS OF OPERATIONS

The Company reported a net loss of $880.5 million in 2008 compared to net income of $180.9 million for 2007, representing a loss per diluted share of $4.71 and earnings per diluted share of $1.17 for 2008 and 2007, respectively.

Net Interest Income

Net interest income is the Company s primary source of revenue. Net interest income represents the difference between interest and fee income generated from earning assets and the interest expense paid on deposits and borrowed funds. Interest rate volatility, which impacts the volume and mix of earning assets and interest bearing liabilities as well as their rates, can significantly impact net interest income. The net interest margin is fully tax equivalent net interest income expressed as a percentage of average earning assets for the period being measured. The net interest margin is presented on a fully tax equivalent basis to consistently reflect income from taxable and tax-exempt loans and securities.

Beginning in late 2007 and early 2008, the yield curve returned to a more normalized level after remaining flat or inverted since late 2005. Short-term rates were driven by rate decreases by the Federal Reserve, while long-term rates were driven by market supply and demand for debt instruments. After remaining constant at 5.25% from June 2006 to September 2007, the Federal Reserve Board lowered the Federal Funds rate resulting in a Federal Funds rate at December 31, 2008 between zero and 0.25%. Due to intense competition for deposits from financial services companies, the cost of funds in the financial sector has not declined in tandem or commensurate with the decrease in the Federal Funds rate. The following table shows the Federal Funds rate and U.S. Treasury yield curve at each quarter end during the past two years.

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For the twelve months ended December 31, 2008, the Company s net interest income, on a tax equivalent basis, decreased $95.6 million, or 12.5%, as compared to the same period of the prior year. The yield on average earning assets decreased 61 basis points more than the decrease in the rate on average interest bearing liabilities causing net interest margin to contract 79 basis points. The impact to net interest income caused by net interest margin contraction was somewhat mitigated by $334.2 million in net proceeds from the issuance of 43.7 million shares of BancGroup common stock in April 2008.

Net interest income was negatively impacted by a 296 basis point decline in the average Wall Street Journal Prime rate and a 258 basis point decline in the average 1 Month LIBOR rate for the twelve months ended December 2008, as compared to the same period of the prior year. For the twelve months ended December 31, 2008 and December 31, 2007, approximately 64% and 63%, respectively, of Colonial s earning assets were variable, adjustable, or short-term in nature. In addition, Colonial s deposit costs did not decline in tandem with the decline in prime and LIBOR rates due to intense competition for deposits from financial services companies. The average cost of deposits exceeded the average Federal Funds rate by at least 57 basis points for the twelve months ended December 31, 2008, as compared to the twelve months ended December 31, 2007, when the average cost of deposits was lower than the average Federal Funds rate by 170 basis points. The spread between the average Federal Funds rate and the average cost of deposits increased throughout 2008 as the average cost of deposits was 26 basis points less than the average Federal Funds rate in the first quarter of 2008 and was 155 basis points greater than the average Federal Funds rate for the fourth quarter of 2008.

In an effort to mitigate the impact to earnings from the Company s asset sensitive balance sheet, Colonial added interest rate floors on certain mortgage warehouse assets during 2008 and slowed the decline in Colonial s base rate. At December 31, 2008, approximately $4.3 billion, or 16.5%, of total assets had a weighted average floor of 5.10%. In addition, Colonial did not reduce its base rate at the same pace as the Wall Street Journal Prime Rate. Colonial s average base rate of 8.05% for 2007 equaled the Wall Street Journal Prime Rate while Colonial s average base rate of 5.71% for 2008 was greater than the Wall Street Journal Prime Rate by 62 basis points. At December 31, 2008, approximately $2.9 billion, or 12.2%, of earning assets were tied to Colonial s base rate of 4.5%. The following table shows average rates for selected balance sheet categories as well as selected market rates:

Analysis of Average Rates

	Twelve Months Ended December 31, 2008	Twelve Months Ended December 31, 2007	Increase/ (Decrease)
Loans, net of unearned income	**6.02%**	7.64%	(1.62)%
Loans held for sale	**5.12%**	6.87%	(1.75)%
Securities	**5.78%**	5.66%	0.12%
Resell agreements & other interest earning assets	**4.50%**	6.67%	(2.17)%
Total interest earning assets	**5.74%**	7.22%	(1.48)%
Interest bearing deposits	**3.16%**	4.06%	(0.90)%
Total deposits	**2.66%**	3.35%	(0.69)%
Wholesale borrowings	**4.30%**	5.07%	(0.77)%
Total interest bearing liabilities	**3.45%**	4.32%	(0.87)%
Federal Funds rate	**2.09%**	5.05%	(2.96)%
1 Month LIBOR	**2.67%**	5.25%	(2.58)%
Wall Street Journal Prime	**5.09%**	8.05%	(2.96)%
Colonial s base rate	**5.71%**	8.05%	(2.34)%

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Interest Earning Assets

Average earning assets increased $2.7 billion, or 12.3%, from 2007. Average earning assets, as shown below, consisted primarily of loans, securities, loans held for sale and securities purchased under agreements to resell (included in other earning assets below). Colonial had a larger proportion of securities, loans held for sale, and securities purchased under agreements to resell for the twelve months ended December 31, 2008, as compared to the same period of the prior year.

Average Funding

Average funding grew $2.9 billion, or 12.2%, for the twelve months ended December 31, 2008, as compared to the same period of the prior year. While average deposits remained fairly consistent, comprising 70% of total funding at December 31, 2008, compared to 69% at December 31, 2007, there was a customer shift from interest bearing non-time deposits into time deposits during 2008.

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The Average Volume and Rates and Analysis of Interest Increases (Decreases) tables present the individual components of net interest income and the net interest margin.

Average Volume and Rates

	2008			2007			2006		
	Average Volume	Interest	Average Rate	Average Volume	Interest (In thousands)	Average Rate	Average Volume	Interest	Average Rate
ASSETS:									
Interest earning assets:									
Loans, net of unearned income[(1)(2)(4)]	**$ 15,454,146**	**$ 930,972**	**6.02%**	$ 15,290,766	$ 1,168,231	7.64%	$ 15,339,699	$ 1,165,917	7.60%
Loans held for sale[(1)(4)]	**2,598,804**	**133,149**	**5.12%**	1,613,170	110,858	6.87%	1,374,115	92,921	6.76%
Held to maturity securities and securities available for sale:									
Taxable[(4)]	**3,245,131**	**189,198**	**5.83%**	2,701,562	150,951	5.59%	2,823,409	141,918	5.03%
Nontaxable[(2)(4)]	**359,021**	**22,746**	**6.34%**	267,212	16,482	6.17%	45,497	2,967	6.52%
Equity securities[(4)]	**207,385**	**8,337**	**4.02%**	202,049	11,977	5.93%	145,547	8,498	5.84%
Total securities[(4)]	**3,811,537**	**220,281**	**5.78%**	3,170,823	179,410	5.66%	3,014,453	153,383	5.09%
Securities purchased under agreements to resell	**2,029,631**	**105,833**	**5.21%**	1,467,233	99,602	6.79%	592,840	40,176	6.78%
Federal funds sold	**80,236**	**1,879**	**2.34%**	84,371	4,158	4.93%	84,912	4,283	5.04%
Interest bearing deposits in banks and the Federal Reserve	**334,294**	**2,183**	**0.65%**	10,504	440	4.19%	3,887	151	3.88%
Total interest earning assets[(2)]	**24,308,648**	**$ 1,394,297**	**5.74%**	21,636,867	$ 1,562,699	7.22%	20,409,906	$ 1,456,831	7.14%
Allowance for loan losses	**(252,594)**			(174,419)			(175,060)		
Cash and due from banks	**377,115**			336,814			376,815		
Premises and equipment, net	**517,874**			449,744			362,142		
Net unrealized loss on available for sale securities	**(194,052)**			(33,880)			(81,613)		
Other assets[(4)]	**2,005,008**			1,630,138			1,345,500		
Total assets	**$ 26,761,999**			$ 23,845,264			$ 22,237,690		
LIABILITIES AND SHAREHOLDERS EQUITY:									
Interest bearing liabilities:									
Interest bearing non-time deposits	**$ 5,461,533**	**$ 94,005**	**1.72%**	$ 5,814,153	$ 184,057	3.17%	$ 4,886,875	$ 137,986	2.82%
Savings deposits	**406,885**	**1,428**	**0.35%**	552,270	7,758	1.40%	1,223,991	33,574	2.74%
Time deposits	**8,146,815**	**331,652**	**4.07%**	6,741,839	335,493	4.98%	6,154,774	272,669	4.43%
Brokered time deposits	**1,573,889**	**65,429**	**4.16%**	473,795	24,405	5.15%	509,611	23,161	4.54%
Reciprocal brokered time deposits	**133,545**	**4,509**	**3.38%**	71,536	3,120	4.36%	43,783	1,899	4.34%
Total brokered time deposits	**1,707,434**	**69,938**	**4.10%**	545,331	27,525	5.05%	553,394	25,060	4.53%
Total interest bearing deposits	**15,722,667**	**497,023**	**3.16%**	13,653,593	554,833	4.06%	12,819,034	469,289	3.66%
Repurchase agreements	**515,089**	**10,360**	**2.01%**	600,176	24,773	4.13%	867,534	37,327	4.30%
Federal funds purchased	**386,965**	**11,616**	**3.00%**	645,686	33,169	5.14%	1,079,743	55,331	5.12%
Other short-term borrowings	**278,578**	**5,539**	**1.99%**	201,167	9,971	4.96%	39,426	2,133	5.41%
Long-term debt[(4)]	**4,059,823**	**197,776**	**4.87%**	3,292,036	172,365	5.24%	2,324,505	136,237	5.86%
Total interest bearing liabilities	**20,963,122**	**$ 722,314**	**3.45%**	18,392,658	$ 795,111	4.32%	17,130,242	$ 700,317	4.09%
Noninterest bearing demand deposits	**2,962,445**			2,912,527			2,969,285		
Other liabilities[(4)]	**278,682**			194,725			145,391		

Total liabilities	**24,204,249**			21,499,910			20,244,918		
Minority interest/REIT preferred securities	**293,058**			179,058					
Shareholders equity	**2,264,692**			2,166,296			1,992,772		
Total liabilities and shareholders equity	**$ 26,761,999**			$ 23,845,264			$ 22,237,690		
RATE DIFFERENTIAL			**2.29%**			2.90%			3.05%
NET INTEREST INCOME AND NET YIELD ON INTEREST EARNING ASSETS ON A TAX EQUIVALENT BASIS(3)		**$ 671,983**	**2.76%**		$ 767,588	3.55%		$ 756,514	3.71%
Taxable equivalent adjustments(2):									
Loans		**(726)**			(830)			(325)	
Held to maturity securities and securities available for sale		**(7,744)**			(5,384)			(922)	
Total taxable equivalent adjustments		**(8,470)**			(6,214)			(1,247)	
Net interest income		**$ 663,513**			$ 761,374			$ 755,267	
TOTAL AVERAGE DEPOSITS:									
Total interest bearing deposits	**$ 15,722,667**	**$ 497,023**	**3.16%**	$ 13,653,593	$ 554,833	4.06%	$ 12,819,034	$ 469,289	3.66%
Noninterest bearing demand deposits	**2,962,445**			2,912,527			2,969,285		
Total average deposits	**$ 18,685,112**	**$ 497,023**	**2.66%**	$ 16,566,120	$ 554,833	3.35%	$ 15,788,319	$ 469,289	2.97%
Total average deposits, excluding brokered time(5)	**$ 17,111,223**	**$ 431,594**	**2.52%**	$ 16,092,325	$ 530,428	3.30%	$ 15,278,708	$ 446,128	2.92%

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(1) Loans and loans held for sale classified as nonaccrual are included in the average volume calculation. Interest income on loans includes loan fees of $33 million, $38 million and $48 million for 2008, 2007 and 2006, respectively.
(2) Interest earned and average rates on securities and loans exempt from income taxes are reflected on a fully tax equivalent basis using a federal income tax rate of 35%, net of nondeductible interest expense.
(3) Net yield on interest earning assets is net interest income divided by average total interest earning assets.
(4) Unrealized gains (losses) on available for sale securities and the adjustments for mark to market valuations on hedged assets and liabilities have been classified in either nonearning assets or other liabilities.
(5) Reciprocal brokered time deposits are not excluded.

Analysis of Interest Increases (Decreases)

	2008 Change From 2007			2007 Change From 2006		
		Attributed To[(1)]			Attributed To[(1)]	
	Amount	Volume	Rate	Amount	Volume	Rate
			(In thousands)			
Interest income:						
Loans, net of unearned income	**$ (237,259)**	**$ 10,451**	**$ (247,710)**	$ 2,314	$ (3,822)	$ 6,136
Loans held for sale	**22,291**	**50,521**	**(28,230)**	17,937	16,425	1,512
Taxable securities	**38,247**	**31,763**	**6,484**	9,033	(6,778)	15,811
Nontaxable securities	**6,264**	**5,810**	**454**	13,515	13,674	(159)
Equity securities	**(3,640)**	**219**	**(3,859)**	3,479	3,348	131
Total securities	**40,871**	**37,792**	**3,079**	26,027	10,244	15,783
Securities purchased under agreements to resell	**6,231**	**29,413**	**(23,182)**	59,426	59,367	59
Federal funds sold	**(2,279)**	**(94)**	**(2,185)**	(125)	(32)	(93)
Interest bearing deposits in banks and the Federal Reserve	**1,743**	**2,116**	**(373)**	289	278	11
Total interest income	**(168,402)**	**130,199**	**(298,601)**	105,868	82,460	23,408
Interest expense:						
Interest bearing non-time deposits	**(90,052)**	**(5,747)**	**(84,305)**	46,071	28,967	17,104
Savings deposits	**(6,330)**	**(531)**	**(5,799)**	(25,816)	(9,415)	(16,401)
Time deposits	**(3,841)**	**57,510**	**(61,351)**	62,824	28,973	33,851
Brokered time deposits	**41,024**	**45,715**	**(4,691)**	1,244	(1,865)	3,109
Reciprocal brokered time deposits	**1,389**	**2,090**	**(701)**	1,221	1,212	9
Repurchase agreements	**(14,413)**	**(1,689)**	**(12,724)**	(12,554)	(11,079)	(1,475)
Federal funds purchased	**(21,553)**	**(7,735)**	**(13,818)**	(22,162)	(22,378)	216
Other short-term borrowings	**(4,432)**	**1,543**	**(5,975)**	7,838	8,016	(178)
Long-term debt	**25,411**	**37,590**	**(12,179)**	36,128	50,540	(14,412)
Total interest expense	**(72,797)**	**128,746**	**(201,543)**	94,794	72,971	21,823
Net interest income	**$ (95,605)**	**$ 1,453**	**$ (97,058)**	$ 11,074	$ 9,489	$ 1,585

(1) Increases (decreases) are attributed to volume changes and rate changes on the following basis: Volume Change = change in volume times old rate. Rate Change = change in rate times old volume. The Rate/Volume Change = change in volume times change in rate, and is included in Volume Change above.

Interest income decreased $168.4 million from 2007. Average earning assets increased $2.7 billion while the yield earned on those assets decreased 148 basis points. The drivers of these changes are more fully described in the following paragraphs.

Interest income on loans decreased $237.3 million compared to 2007. The decrease was primarily due to the decrease in the prime lending rate and an increase in average nonperforming loans which resulted in the average yield earned on loans decreasing 162 basis points.

Interest income on loans held for sale increased $22.3 million compared to 2007. The average volume of loans held for sale increased $985.6 million, or 61.1%, primarily from an increase in loans held for sale in the Company s mortgage warehouse division. The increase in volume was partially offset by a decrease in the yield on loans held for sale, which decreased 175 basis points to 5.12% from 6.87% in the same period of the prior year. The yield is driven by the prevailing market rates which were significantly lower in 2008 than in 2007. Certain of the loans held for sale contain floors which prevented the yield on these assets from decreasing further.

Interest income on securities increased $40.9 million compared to 2007. The increase was primarily the result of a $640.7 million, or 20.2%, increase in average volume, as well as a 12 basis point increase in yield on the average balances.

Interest income from securities purchased under agreements to resell increased $6.2 million from 2007. The average volume of securities purchased under agreements to resell increased $562.4 million, or 38.3%, primarily from growth in the Company s mortgage warehouse division. The yield on securities purchased under agreements to resell decreased 158 basis points to 5.21% from 6.79% in the prior year. The yield is driven by the prevailing market rates which were significantly lower in 2008 than in 2007. Certain of the securities purchased under agreements to resell contain floors which prevented the yield on these assets from decreasing further.

Interest expense decreased approximately $72.8 million from 2007. The decrease in interest expense was driven primarily by an 87 basis point decrease in the cost of average interest bearing liabilities which was partially offset by a $2.6 billion, or 14.0%, increase in average interest bearing liabilities. The drivers of the decrease in funding costs are described in the following paragraphs.

Interest expense on interest bearing non-time deposits decreased $90.1 million compared to 2007. The decrease in interest expense was due to a rate reduction of 145 basis points and an average volume decrease of $352.6 million, or 6.1%. During 2008, customer preference shifted away from interest bearing non-time deposits towards time deposits, thereby reducing the average balances in these accounts.

Interest expense on savings deposits decreased $6.3 million from 2007. The decrease in interest expense was primarily due to an interest rate decrease of 105 basis points and an average volume decrease of $145.4 million, or 26.3%. During 2008, customer preference shifted away from savings deposits towards time deposits, thereby reducing the average balances in these accounts.

Interest expense on time deposits decreased $3.8 million compared to 2007. The decrease in interest expense was due to an interest rate decrease of 91 basis points which was partially offset by an average volume increase of $1.4 billion, or 20.8%. The growth of time deposits is attributable to customer preference for higher rate products and increased competition for deposits as a funding source.

Interest expense on brokered time deposits increased $42.4 million compared to 2007. The increase in interest expense was due to an increase in average volume of $1.2 billion, or 213.1%, which was partially offset by an interest rate decrease of 95 basis points. The volume increase was due to the Company s increased use of brokered time deposits as a funding source.

Interest expense on short-term borrowings decreased $40.4 million from 2007. The decrease in interest expense was primarily due to an interest rate decrease of 236 basis points and an average volume decrease of $266.4 million, or 18.4%. As the Company has continued to deleverage its balance sheet, it has reduced the need for short-term borrowings.

Interest expense on long-term debt increased $25.4 million compared to 2007. The increase in interest expense was primarily caused by an increase in average long-term debt of $767.8 million, or 23.3%, partially offset by an interest rate decrease of 37 basis points. Colonial issued $250 million in subordinated debt during the

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first quarter of 2008 causing average long term debt to increase $205.6 million over 2007. Average Federal Home Loan Bank of Atlanta (FHLB) borrowings increased $628.2 million over 2007 as the Company increased its use of FHLB borrowings as a funding source.

Loan Loss Provision

The provision for loan losses for the year ended December 31, 2008 was $728.9 million compared to $106.5 million for 2007. The provision for loan losses exceeded net charge-offs by $86.2 million and $52.4 million for the years ended December 31, 2008 and 2007, respectively. Net charge-offs were $642.8 million and $54.1 million for the years ended December 31, 2008 and 2007, respectively. During 2008, approximately $427 million of troubled assets were sold at a 58% discount, which was a significant driver of the increase in net charge-offs for the year.

At December 31, 2008, BancGroup s allowance for loan losses was $325.0 million, up $86.2 million over December 31, 2007. The allowance for loan losses represented 2.24% of period end net loans at December 31, 2008 compared to 1.50% at December 31, 2007. For more information, refer to the *Allowance for Loan Losses* discussion presented in the *Risk Management* section of Management s Discussion and Analysis.

Noninterest Income

The following charts detail the Company s core noninterest income by category for the years ended December 31, 2008 and 2007:

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The following table shows the dollar and percentage change in noninterest income by category for 2008 as compared to 2007, and 2007 as compared to 2006. Core noninterest income decreased $8.6 million, or 4%, in 2008 as compared to 2007.

	Year Ended December 31,			Increase (Decrease)			
	2008	2007	2006	2008 Compared to 2007	%	2007 Compared to 2006	%
				(In thousands)			
Service charges on deposit accounts	**$ 76,058**	$ 75,466	$ 65,071	$ 592	0.8%	$ 10,395	16.0%
Electronic banking	**20,363**	18,815	17,212	1,548	8.2	1,603	9.3
Other retail banking fees	**9,417**	12,275	14,436	(2,858)	(23.3)	(2,161)	(15.0)
Retail banking fees	**105,838**	106,556	96,719	(718)	(0.7)	9,837	10.2
Mortgage banking origination and sales	**29,951**	14,923	13,540	15,028	100.7	1,383	10.2
Wealth management services	**17,930**	16,734	14,054	1,196	7.2	2,680	19.1
Mortgage warehouse fees	**5,235**	22,240	25,323	(17,005)	(76.5)	(3,083)	(12.2)
Bank-owned life insurance	**19,395**	20,230	15,954	(835)	(4.1)	4,276	26.8
Other income	**22,504**	28,750	16,031	(6,246)	(21.7)	12,719	79.3
Core noninterest income	**200,853**	209,433	181,621	(8,580)	(4.1)	27,812	15.3
Securities and derivatives gains (losses), net	**3,043**	4,047	4,772	(1,004)	(24.8)	(725)	(15.2)
Securities restructuring charges		(36,006)		36,006	100.0	(36,006)	(100.0)
Gain on sale of mortgages and businesses		8,750	2,829	(8,750)	(100.0)	5,921	209.3
Total noninterest income	**$ 203,896**	$ 186,224	$ 189,222	$ 17,672	9.5%	$ (2,998)	(1.6)%

Service charges on deposit accounts increased 1% over 2007. Service charges on deposit accounts are comprised of nonsufficient funds fees and service charges on consumer and commercial deposit accounts. Noninterest income from service charges on deposit accounts increased, as compared to the prior year, primarily due to an increase in the number of customer accounts as well as customers maintaining lower balances in those accounts.

Electronic banking includes fees from Colonial s ATM network, business and personal check card services and internet banking. Noninterest income from electronic banking services increased 8% from 2007 to 2008 primarily due to an increase in the number of Colonial customer accounts as well as the Company s focused efforts to increase customer check card usage and ATM network fees.

Other retailing banking fees decreased from 2007 to 2008 by $2.9 million. Official check commissions represent $2.4 million of the decrease from prior year primarily due to a decrease in rate. The remainder of the decline from 2007 to 2008 is the result of a decline in merchant services revenue due to the Company s sale of its merchant services contracts in April 2007 and the subsequent agent bank agreement with a third party service provider of merchant services. The outsourced relationship lowers Colonial s inherent risk of providing merchant services while enabling the Company to continue to offer those services to its customer base. The referral fees for new contracts are less than the previous fee income, but the Company s expenses and risks are also reduced. As part of the sale, Colonial recognized a $4.9 million gain in 2007 as noted separately in the table above.

Mortgage banking origination and sales revenue is derived from mortgage loans originated and subsequently sold in the secondary market. The Company does not retain any servicing rights related to these loans. Mortgage banking origination and sales income increased 100.7% from 2007 to 2008, with a 39% increase in sales volume,

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primarily due to a team of mortgage originators hired in late 2007. In addition, profit margins improved due to a shift to higher margin FHA and VA products from other products and enhanced controls over pricing and delivery.

Wealth management services include discount brokerage, investment sales, asset management, trust services and insurance sales including term, universal, whole life and long-term care. Wealth management services increased $1.2 million from 2007 to 2008 primarily due to increased volumes in fixed annuity products sold, partially offset by a decline in the volume of variable annuities and securities sold and in trust revenues. The increased volumes of fixed annuities were driven by customer demand and uncertainty in the financial markets.

Mortgage warehouse fees are comprised of three revenue streams: custodial fees associated with mortgage document services for mortgage warehouse customers, syndication fees paid to the Company as agent or participant in mortgage warehouse syndicated loans and servicing and other fees associated with interests in mortgage warehouse assets sold to third-party commercial paper conduits (conduits). The decrease of $17.0 million in mortgage warehouse fees from 2007 to 2008 was primarily related to lower servicing and other fees associated with interests sold because Colonial discontinued the sales of assets to the conduits in early January 2008.

Income from bank-owned life insurance (BOLI) decreased from 2007 to 2008 primarily due to lower crediting rates.

Other income reflects revenues from joint ventures, letter of credit fees, condo association coupon fees, gains on the sales of bank premises and other assets and several other small items. The decrease from 2007 to 2008 was primarily the result of a $10.0 million decline in revenue from joint ventures as well as a $2.7 million decrease in gains related to the sale of bank premises, partially offset by a $2.1 million gain on the sale of Visa, Inc. stock from the initial public offering, a $1.5 million increase in equity investment income and a $526,000 increase in the fair value of retail mortgage forward sale commitments.

The Company s decision to buy and sell securities is based on its management of interest rate risk and projected liquidity and funding needs. During 2008, the Company recorded gains of $6.1 million in the first quarter from the sale of approximately $217 million in securities, a $3.0 million gain in the second quarter from the early termination of a $250 million resell agreement, and a loss of $4.9 million on the sale of Wachovia stock, $658,000 on a derivative swap transaction and a $489,000 write-down of securities in the third quarter. In the first quarter of 2007, the Company recorded gains of $981,000 on the sale of $163 million in securities and recognized an impairment loss of $36.0 million as the Company declared its intent to restructure its securities portfolio by selling approximately $1.2 billion in available for sale securities. The securities were sold in April 2007. In the second quarter of 2007, the Company recorded gains of $1.1 million from the sale of additional available for sale debt securities and equity securities.

The Company sold approximately $490 million of residential real estate loans in March 2007 and recognized a $3.9 million gain.

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Noninterest Expense

The following charts detail the Company s core noninterest expense by category for the years ended December 31, 2008 and 2007:

(1) Other consists of other expenses and any category of core noninterest expense that falls below 5% of total core noninterest expense.

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The following table shows the dollar and percentage changes in noninterest expense by category for 2008 as compared to 2007, and 2007 as compared to 2006. Core noninterest expense increased $117.0 million, or 21.6%, in 2008 as compared to 2007. Core noninterest expense to average assets was 2.46% and 2.27% for 2008 and 2007, respectively.

	Year Ended December 31,			Increase (Decrease)			
	2008	2007	2006	2008 Compared to 2007	%	2007 Compared to 2006	%
			(In thousands)				
Salaries and employee benefits	**$ 295,881**	$ 279,055	$ 279,612	$ 16,826	6.0%	$ (557)	(0.2)%
Occupancy expense of bank premises, net	**95,485**	78,709	67,338	16,776	21.3	11,371	16.9
Furniture and equipment expenses	**59,865**	53,262	48,585	6,603	12.4	4,677	9.6
Professional services	**29,112**	18,787	18,465	10,325	55.0	322	1.7
FDIC insurance and other regulatory fees	**18,081**	6,301	4,822	11,780	187.0	1,479	30.7
Amortization of intangible assets	**16,613**	13,358	12,209	3,255	24.4	1,149	9.4
Electronic banking and other retail banking expenses	**16,043**	19,660	13,521	(3,617)	(18.4)	6,139	45.4
Losses and expenses on other real estate	**28,366**	1,171	854	27,195	2322.4	317	37.1
Loss on equity investments	**16,925**	3,019	1,514	13,906	460.6	1,505	99.4
Advertising	**12,092**	10,065	10,782	2,027	20.1	(717)	(6.6)
Communications	**11,371**	11,099	10,845	272	2.5	254	2.3
Postage and courier	**9,896**	10,656	10,476	(760)	(7.1)	180	1.7
Loan closing costs	**6,628**	5,549	5,067	1,079	19.4	482	9.5
Travel	**6,525**	6,945	8,200	(420)	(6.1)	(1,255)	(15.3)
Other expenses	**36,266**	24,503	26,898	11,763	48.0	(2,395)	(8.9)
Core noninterest expense	**659,149**	542,139	519,188	117,010	21.6	22,951	4.4
Goodwill impairment	**575,000**			575,000	100.0		
Severance expense	**786**	6,616	413	(5,830)	(88.1)	6,203	1501.9
Merger related expenses		4,015		(4,015)	(100.0)	4,015	100.0
Net loss related to the early extinguishment of debt	**10,327**	6,908		3,419	49.5	6,908	100.0
Total noninterest expense	**$ 1,245,262**	$ 559,678	$ 519,601	$ 685,584	122.5%	$ 40,077	7.7%

Salaries and employee benefits increased 6% from 2007 to 2008. The change was primarily due to a decrease in deferred salary costs and increases in commissions and separation payments along with an additional working day in 2008. Stock-based compensation expense decreased from 2007 due to certain performance criteria not being met, resulting in the reversal of previously expensed performance-based restricted stock. The Company s average number of full-time equivalent employees increased from 4,588 in 2007 to 4,671 in 2008. The increase in employees was primarily due to the Company s two acquisitions in 2007, but was partially offset by reductions in workforce in 2007 and 2008.

The increases in occupancy and furniture and equipment expenses were primarily due to the 2007 acquisitions of Commercial Bankshares, Inc. and Citrus and Chemical Bancorporation, Inc. Additional increases resulted from higher information technology costs, charges related to abandoned leases and increased lease expense resulting from the sale-leaseback of 56 properties in 2007. The increased occupancy expense from the sale-leasebacks is more than offset by the amortization of deferred gains on the sales, which are included in noninterest income.

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Professional services increased from 2007 to 2008 primarily due to increases in legal fees associated with credit related matters, accounting fees, consulting fees related to the Colonial 1st Project and technology related services.

FDIC insurance and other regulatory fees increased from 2007 to 2008 due to increases in deposits on which the FDIC assessment is based, as well as the depletion of Colonial Bank s available FDIC assessment credits in late 2007.

Amortization of intangible assets increased from 2007 to 2008 due to additional core deposit intangible assets that were recorded for the Commercial Bankshares, Inc. and Citrus & Chemical Bancorporation, Inc. acquisitions in 2007.

Electronic banking and other retail banking expenses decreased from 2007 to 2008 due to the discontinuance of consulting services related to revenue enhancement initiatives, as well as management s focused efforts to reduce fraud and operating losses.

The increases in losses and expenses on other real estate were driven by higher charges resulting from real estate value declines arising from the current U.S. recession. The losses and expenses on other real estate for 2008 included $4.8 million of write downs on properties sold, $11.7 million of additional write downs on other real estate and $11.9 million in other real estate expenses.

Loss on equity investments increased from 2007 to 2008 due to the recognition of $10.4 million of impairment charges during 2008 along with operating losses related to real estate joint ventures and low income housing tax credit investments, as well as the establishment of a $1.5 million reserve for losses.

Advertising expense increased from 2007 to 2008 primarily due to increased newspaper and radio advertisements to attract and retain deposits.

Loan closing costs increased from 2007 to 2008 primarily due to the increased frequency of appraisals driven by rapid declines in real estate values in late 2007 and throughout 2008.

Other expenses increased from 2007 to 2008 primarily due to an $8.6 million increase in subservicing fees associated with the increased balances of mortgage warehouse assets, an increase in the off-balance sheet credit reserve of $2.0 million and a charge of $1.1 million related to a litigation settlement.

Colonial recorded a noncash charge of $575.0 million in the fourth quarter of 2008 for goodwill impairment. Goodwill recorded on past acquisitions in Florida and Nevada became impaired in the fourth quarter primarily due to declining bank market valuations and increased credit costs. Refer to the *Goodwill* section of Management s Discussion and Analysis for additional information.

Severance expense relates primarily to the reduction in force efforts in 2007. This expense decreased significantly for 2008.

Merger related expenses in 2007 related to the acquisitions of Commercial Bankshares, Inc. and Citrus & Chemical Bancorporation, Inc.

During 2008, the Company incurred a $10.3 million net loss related to the early extinguishment of debt. A $9.7 million loss was incurred on the early termination of $205 million in FHLB advances, which bore interest averaging 4.68%, and a $597,000 loss was incurred on the call of $90.5 million in brokered time deposits, which bore interest at 4.90%. During 2007, the Company redeemed $185 million of trust preferred securities, which bore interest averaging 8.58%, and incurred a $6.9 million net loss related to the early extinguishment of debt.

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Minority Interest Expense/REIT Preferred Dividends

During May 2007, the Company issued $300 million in fixed-to-floating rate perpetual non-cumulative preferred stock through its indirect subsidiary CBG Florida REIT Corp. These securities pay dividends at a rate of 7.114% until May 15, 2012 and 3-month LIBOR plus 2.02% for each dividend period thereafter. The dividends are reflected, before tax, as minority interest expense on the Company s consolidated statements of income. CBG Florida REIT Corp. may redeem the preferred stock, in whole or in part, on May 15, 2012 and each fifth succeeding year thereafter. Refer to Note 20, *Minority Interest/REIT Preferred Securities,* for additional information.

Provision for Income Taxes

The effective income tax rate was 22.0% in 2008 and 32.6% in 2007. During 2008, the loss recognized created an income tax benefit of $247.7 million. The provision for income taxes in 2007 was $87.6 million. The decrease in the effective tax rate from 2007 was primarily the result of substantial losses recognized during 2008, which was partially offset by the impairment of goodwill, much of which was a non-taxable charge. For further information concerning the provision for income taxes, refer to Note 25, *Income Taxes*.

REVIEW OF STATEMENT OF CONDITION

Financial Condition

Changes in selected components of the Company s balance sheet from December 31, 2007 to December 31, 2008 are as follows:

	December 31, 2008	December 31, 2007	Increase (Decrease) $	%
		(Dollars in thousands)		
Interest bearing deposits in banks and the Federal Reserve	**$ 1,534,463**	$ 28,993	$ 1,505,470	5,192.5%
Securities purchased under agreements to resell	**1,556,157**	2,049,664	(493,507)	(24.1)
Securities	**3,503,380**	3,682,510	(179,130)	(4.9)
Loans held for sale	**2,082,248**	1,544,222	538,026	34.8
Loans, net of unearned income	**14,530,018**	15,923,178	(1,393,160)	(8.7)
Goodwill	**432,053**	1,008,168	(576,115)	(57.1)
Other real estate owned	**127,850**	15,760	112,090	711.2
Total assets	**25,816,306**	25,975,989	(159,683)	(0.6)
Non-time deposits	**7,989,907**	9,771,573	(1,781,666)	(18.2)
Total deposits	**18,673,265**	18,544,267	128,998	0.7
Short-term borrowings	**1,172,706**	568,721	603,985	106.2
Long-term debt	**4,043,807**	4,023,836	19,971	0.5
Minority interest/REIT preferred securities	**293,058**	293,058	0	0.0
Shareholders equity	**1,344,978**	2,273,571	(928,593)	(40.8)

Interest Bearing Deposits in Banks and the Federal Reserve

In response to significant uncertainty in the marketplace and to increase liquid assets, Colonial increased the level of cash balances maintained at the Federal Reserve and the FHLB, thereby increasing interest bearing deposits in banks and the Federal Reserve to $1.5 billion as of December 31, 2008 as compared to $29 million at December 31, 2007. The balance held at the Federal Reserve at December 31, 2008 was $1.1 billion while the balance held at the FHLB was $388.5 million.

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Securities Purchased Under Agreements to Resell

Colonial s securities purchased under agreements to resell at December 31, 2008 represent mortgage backed securities which have been securitized by customers of the Company s mortgage warehouse lending division and are under agreements to be sold to third-party investors. Colonial purchases these securities prior to their initial settlements with those investors. Refer to the *Mortgage Warehouse Assets* section of Management s Discussion and Analysis for additional information. At December 31, 2007, Colonial had an additional $500 million invested in traditional resell agreements that were terminated during 2008.

Securities

BancGroup determines the funds available for investment based upon anticipated loan and deposit growth, liquidity needs and pledging requirements, as well as other factors. An investment strategy is developed based on these factors, along with BancGroup s balance sheet position and relative value opportunities in the market.

All securities are either classified as held to maturity or available for sale. Held to maturity securities are those securities which management has the ability and intent to hold until maturity. The carrying value of held to maturity securities was $200.4 million at the end of 2008 compared to $1.2 million at the end of 2007. The current year increase was the result of purchases during 2008. Securities classified as held to maturity consisted primarily of agency mortgage-backed securities and included U.S. Treasury bonds and municipal obligations. The following chart details the Company s held to maturity securities at December 31, 2008 by category:

Held To Maturity Securities

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Securities available for sale represent those securities that the Company intends to hold for an indefinite period of time and may be sold in response to changes in BancGroup s interest rate risk position, prepayment risk or other similar factors. These securities are recorded at fair value with unrealized gains or losses, net of any tax effect, added to or deducted from shareholders equity. At December 31, 2008, the net unrealized pretax loss on securities available for sale was $476.9 million, compared to $5.8 million at December 31, 2007. The unrealized loss, net of income taxes, is reflected in the Company s shareholders equity in the amount of $310.0 million and $3.7 million at December 31, 2008 and 2007, respectively. At December 31, 2008, securities available for sale totaled $3.3 billion, or 94.3% of the total securities portfolio, compared to $3.7 billion, or 99.97%, at December 31, 2007. The following chart details the Company s securities available for sale at December 31, 2008 by category:

The composition of the Company s securities portfolio is reflected in the following tables.

Securities by Category

	Carrying Value at December 31,		
	2008	**2007**	**2006**
		(In thousands)	
Securities available for sale:			
U.S. Treasury securities and obligations of U.S. government sponsored entities (GSE s)	**$ 25,222**	$	$ 166,481
Agency mortgage-backed securities	**1,533,391**	1,359,503	1,012,855
Non-agency mortgage-backed securities	**1,203,263**	1,701,047	1,670,973
Obligations of state and political subdivisions	**345,695**	371,930	78,603
Corporate notes		6,819	
Federal Reserve and FHLB stock and other	**195,388**	241,983	154,702
Total securities available for sale	**3,302,959**	3,681,282	3,083,614
Held to maturity securities:			
U.S. Treasury securities	**500**	500	500
Agency mortgage-backed securities	**199,687**	495	747
Obligations of state and political subdivisions	**234**	233	627
Total held to maturity securities	**200,421**	1,228	1,874
Total securities	**$ 3,503,380**	$ 3,682,510	$ 3,085,488
Securities to total assets	**13.6%**	14.2%	13.5%
Average securities to average earning assets	**15.7%**	14.7%	14.8%
Average duration (excluding equities)	**5.71 years**	4.97 years	4.45 years

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Securities by Credit Rating at December 31, 2008

	Government / GSE Obligations	Lower of Standard & Poor s or Moody s Designation AAA	A-to AA+	BBB-to BBB+	Unrated/ Other	Total
		(In thousands)				
U.S. Treasury securities and obligations of U.S. GSE s	**$ 25,722**	**$**	**$**	**$**	**$**	**$ 25,722**
Agency mortgage-backed securities	**1,733,078**					**1,733,078**
Non-agency mortgage-backed securities		**653,576**	**264,589**	**148,509**	**136,589**	**1,203,263**
Obligations of state and political subdivisions		**24,060**	**305,442**	**14,082**	**2,345**	**345,929**
FHLB stock and other		**19,511**			**175,877**	**195,388**
Total securities	**$ 1,758,800**	**$ 697,147**	**$ 570,031**	**$ 162,591**	**$ 314,811**	**$ 3,503,380**

As of December 31, 2008, the ratings for approximately $136.6 million of securities in Colonial s portfolio were reduced to below investment grade by the rating agencies due to deteriorating U.S. economic conditions. Colonial still expects to collect all contractual principal and interest amounts on these securities.

Securities by Credit Rating at December 31, 2007

	Government / GSE Obligations	Lower of Standard & Poor s or Moody s Designation AAA	A-to AA+	BBB-to BBB+	Unrated/ Other	Total
		(In thousands)				
U.S. Treasury securities	$ 500	$	$	$	$	$ 500
Agency mortgage-backed securities	1,359,998					1,359,998
Non-agency mortgage-backed securities		1,701,047				1,701,047
Obligations of state and political subdivisions		367,136	2,321		2,706	372,163
Federal Reserve and FHLB stock and other			4,965	1,856	241,981	248,802
Total securities	$ 1,360,498	$ 2,068,183	$ 7,286	$ 1,856	$ 244,687	$ 3,682,510

Securities by Credit Rating at December 31, 2006

	Government / GSE Obligations	Lower of Standard & Poor s or Moody s Designation AAA	A-to AA+	BBB-to BBB+	Unrated/ Other	Total
		(In thousands)				
U.S. Treasury securities	$ 166,981	$	$	$	$	$ 166,981
Agency mortgage-backed securities	1,013,602					1,013,602
Non-agency mortgage-backed securities		1,670,973				1,670,973
Obligations of state and political subdivisions		72,965	2,258		4,007	79,230
Federal Reserve and FHLB stock and other					154,702	154,702
Total securities	$ 1,180,583	$ 1,743,938	$ 2,258	$	$ 158,709	$ 3,085,488

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The maturities of the Company s debt securities portfolio at December 31, 2008 are as follows:

Contractual Maturity Distribution of Debt Securities[(1)]

	Within 1 Year		1-5 Years		5-10 Years		Over 10 Years	
	Amount	Average Rate	Amount	Average Rate	Amount	Average Rate	Amount	Average Rate
	(In thousands)							
Securities available for sale:								
U.S Treasury securities and obligations of GSE s	$	%	$	%	$ 25,222	3.00%	$	%
Agency mortgage-backed securities	36	5.50%	1,313	6.14%	45,849	5.68%	1,486,192	5.55%
Non-agency mortgage-backed securities		%		%		%	1,203,263	6.06%
Obligations of state and political subdivisions[(2)]	1,802	6.99%	9,124	6.40%	60,556	6.31%	274,363	6.33%
Federal Reserve and FHLB stock and other		%		%		%		%
Total securities available for sale	1,838	6.96%	10,437	6.37%	131,627	5.46%	2,963,818	5.83%
Held to maturity securities:								
U.S. Treasury securities		%		%	500	7.25%		%
Agency mortgage-backed securities	5	10.01%	55	7.01%	92	8.53%	199,535	5.89%
Obligations of state and political subdivisions[(2)]		%	234	7.76%		%		%
Total held to maturity securities	5	10.01%	289	7.62%	592	7.45%	199,535	5.89%
Total debt securities	$ 1,843	6.97%	$ 10,726	6.40%	$ 132,219	5.47%	$ 3,163,353	5.83%

(1) These are contractual maturities; expected and actual maturities could differ from contractual maturities because underlying borrowers may have the right to call or prepay obligations without call or prepayment penalties.

(2) The weighted average yields are calculated on the basis of the cost and effective yield weighted for the scheduled maturity of each security. The yield is reflected on a fully tax equivalent basis using a federal income tax rate of 35%, net of nondeductible interest expense.

Mortgage Warehouse Assets

The mortgage warehouse lending division provides short-term, secured funding to mortgage companies. Colonial s fundings to the mortgage companies are reflected in loans, loans held for sale and securities purchased under agreements to resell. The mortgage warehouse assets are secured by mortgage loans that are sold to investors such as Fannie Mae, Freddie Mac, Ginnie Mae and money center financial institutions who have committed to purchase the mortgage loans collateralizing the mortgage warehouse assets. The mortgage loans are generally delivered to investors within one month. Colonial controls the collateral files (which include the underlying mortgage legal documents) for the majority of the outstanding mortgage warehouse assets. In the event of a default by a mortgage company, Colonial could assume ownership of the underlying individual mortgage loan and the related forward sales commitment pursuant to which Colonial could deliver the loan to the permanent investor. During 2008, Colonial s mortgage warehouse lending division provided approximately $70 billion of interim funding to the industry representing nearly 400,000 residential mortgage loans.

Mortgage warehouse loans represent collateralized draws on lines of credit to mortgage origination companies. The loans are used to originate mortgage loans to their customers. Investors have committed to purchase the mortgage loans securing the mortgage warehouse loans. Short-term participations in loans held for sale are another source of funding provided to these companies whereby Colonial purchases participations in certain mortgage loans which have commitments to be sold to third-party investor institutions. Securities purchased under agreements to resell represent mortgage backed securities which have been securitized by these companies and are under agreements to be sold to third-party investors. Colonial purchases these securities prior to their initial settlements with those investors.

Colonial had a facility in which it sold certain mortgage warehouse loans and short-term participations in loans held for sale to a wholly-owned special purpose entity which then sold interests in those assets to third-party commercial paper conduits (conduits). The Company reduced the interests in mortgage warehouse assets that were sold by $500 million in each of April and November 2007, for a total 2007 reduction of $1.0 billion. At December 31, 2007, the total outstanding balances of interests sold to the conduits was $1.0 billion. In January 2008, the balance outstanding to the conduits was reduced to $0 and the facility was terminated by its terms. Refer to Note 9, *Sales and Servicing of Financial Assets*, for additional information.

A summary of the major components of mortgage warehouse assets is shown in the table below:

	December 31, 2008	December 31, 2007
	(In thousands)	
Securities purchased under agreements to resell	**$ 1,556,157**	$ 1,549,664
Loans held for sale	**1,975,654**	1,484,502
Mortgage warehouse loans	**731,176**	290,603
Total mortgage warehouse assets on balance sheet	**4,262,987**	3,324,769
Interests sold:		
Loans held for sale		769,221
Mortgage warehouse loans		230,779
Total mortgage warehouse assets under management	**$ 4,262,987**	$ 4,324,769

Loans Held for Sale

Loans held for sale is comprised of three elements: short-term participations in mortgage loans, retail mortgages and other loans held for sale. Total loans held for sale at December 31, 2008 increased $538 million, or 34.8%, from December 31, 2007, primarily due to an increase in participations purchased by the mortgage warehouse division driven by customer demand and the elimination of the sales of participations to the third party commercial paper conduits, as well as an increase in other loans held for sale. Loans held for sale fluctuate as demand for residential mortgages changes and customer demands change. A summary of the elements that make up loans held for sale is shown in the table below:

	December 31, 2008	December 31, 2007
	(In thousands)	
Short-term participations in mortgage loans held for sale (includes $1,950,445 measured at fair value at December 31, 2008)	**$ 1,975,654**	$ 1,484,502
Retail mortgage loans held for sale	**57,396**	59,720
Other loans held for sale	**49,198**	
Total loans held for sale	**$ 2,082,248**	$ 1,544,222

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BancGroup elected the fair value option for its short-term participations in mortgage loans held for sale acquired on or after August 1, 2008. The fair value of loans held for sale is based on what secondary markets are currently offering for portfolios with similar characteristics. For a detailed discussion of the determination of fair value for individual financial instruments, see Note 5, *Fair Value Measurements.*

Loans

During 2008, Colonial and many other financial institutions became focused on capital preservation. As credit quality in the industry deteriorated and the current U.S. recession severely impacted property values, Colonial s focus shifted from balance sheet growth to balance sheet contraction, or deleveraging. Colonial focused on reducing exposures in specific markets and to specific borrowers. The result of these factors is a $1.8 billion, or 11.7%, decrease in Colonial s outstanding loan portfolio, excluding mortgage warehouse lending, from December 31, 2007 to December 31, 2008. The impact has been most noticeable in the residential construction market. As the current U.S. recession s impact on real estate values has negatively impacted developers and other borrowers, Colonial has been, and continues to be, more selective in approving new loans or expansions of existing loan relationships. Loans in the mortgage warehouse division increased $440.6 million from December 31, 2007. Mortgage warehouse loans increased because Colonial stopped selling interests in mortgage warehouse loans to third-party commercial paper conduits and terminated the off balance sheet facility in January 2008.

Gross Loan Portfolio

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			December 31,		
	2008	2007	2006	2005	2004
			(In thousands)		
Commercial, financial and agricultural	**$ 1,713,267**	$ 1,506,986	$ 1,440,448	$ 1,591,195	$ 2,123,664
Commercial real estate	**4,935,944**	5,012,773	4,291,979	4,424,465	4,270,817
Real estate construction	**4,922,190**	6,296,262	6,340,324	5,483,424	3,936,800
Residential real estate	**2,572,077**	2,673,823	2,987,212	3,048,007	2,228,648
Consumer and other	**402,070**	452,642	438,375	372,470	315,386
Total loans	**14,545,548**	15,942,486	15,498,338	14,919,561	12,875,315
Less: unearned income	**(15,530)**	(19,308)	(19,449)	(19,697)	(17,504)
Total loans, net of unearned income	**$ 14,530,018**	$ 15,923,178	$ 15,478,889	$ 14,899,864	$ 12,857,811

Loans classified as commercial, financial and agricultural represented 11.8% of total loans at December 31, 2008, and consisted of secured and unsecured credit lines and amortizing loans for various industrial, agricultural, commercial, financial, retail or service businesses, as well as mortgage warehouse lines of credit.

Commercial real estate loans represented 33.9% of total loans at December 31, 2008. These loans are collateralized by seasoned real estate held for investment and business purposes.

Real estate construction loans were 33.8% of total loans at December 31, 2008. Loans of this type are made to individuals, companies or developers for use in the purchase or construction of properties such as single and multi-family residential and non-residential real estate. These loans are repaid by the cashflows generated through the operation, sale or refinancing of the underlying commercial property.

Residential real estate loans represented 17.7% of total loans at December 31, 2008. The majority of Colonial s residential real estate loans are adjustable and fixed rate first mortgages on single-family, owner-occupied properties.

Consumer and other loans represented 2.8% of total loans at December 31, 2008. Loans in this category may be unsecured or secured and include loans for investment purposes, vehicle purchases, purchases of personal property, personal expense loans and overdrafts of deposit accounts. These loans are made to individuals and businesses such as financial institutions, municipalities and not-for-profit organizations.

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The contractual maturities of loans may vary significantly from actual maturities due to loan extensions, early payoffs due to refinancing and other factors. Fluctuations in interest rates and availability of credit from other sources are major factors in early loan payoffs. The uncertainties of future events, particularly with respect to interest rates, make it difficult to predict the actual maturities. The following table represents the contractual maturities of loans at December 31, 2008:

Loan Maturity/Rate Sensitivity

		Maturing		Rate Sensitivity		Rate Sensitivity, Loans Maturing Over 1 Year	
	Within 1 Year	1-5 Years	Over 5 Years	Fixed	Floating/ Adjustable	Fixed	Floating/ Adjustable
			(Dollars in thousands)				
Commercial, financial and agricultural	$ 1,255,467	$ 284,490	$ 173,310	$ 366,042	$ 1,347,225	$ 225,141	$ 232,659
Commercial real estate	1,241,636	2,446,233	1,248,075	2,978,002	1,957,942	2,365,264	1,329,044
Real estate construction	3,141,352	1,568,945	211,893	1,087,143	3,835,047	505,663	1,275,175
Residential real estate	1,059,969	909,912	602,196	654,337	1,917,740	269,591	1,242,517
Consumer and other loans	99,231	130,144	172,695	292,356	109,714	227,459	75,380
Totals	$ 6,797,655	$ 5,339,724	$ 2,408,169	$ 5,377,880	$ 9,167,668	$ 3,593,118	$ 4,154,775

For additional discussion of loans, refer to the *Risk Management* section of Management s Discussion and Analysis.

Goodwill

The Company s annual goodwill impairment test was performed as of September 30, 2008. As a result of the annual impairment test, even though four reporting units were required to perform a second step analysis, management determined that no goodwill impairment charge was required at that time, as the implied fair value of goodwill for each tested reporting unit exceeded its carrying value. Due to the decline in market valuations for financial institutions, including Colonial, and increased credit costs during the fourth quarter of 2008, an interim impairment test was performed as of December 31, 2008. As a result of the interim impairment test, the Company computed and recorded a $575.0 million goodwill impairment loss in the fourth quarter of 2008, reducing the balance of goodwill to the implied fair value from the second step of the impairment test. The impairment impacted two of the Company s six reportable segments, representing four of the Company s seven reporting units. Refer to Note 14, *Goodwill and Other Intangible Assets*, as well as the *Purchase Accounting and Goodwill* section of *Critical Accounting Polices* in Management s Discussion and Analysis for additional information.

Due to the ongoing uncertainty in market conditions, which may continue to negatively impact the performance of BancGroup s reporting units as well as the market valuations of financial institutions, including Colonial, management will continue to monitor and evaluate the carrying value of goodwill. Additional goodwill impairment could be recorded in future periods and such impairment could be material to the Company s results of operations.

Other Real Estate Owned

Total other real estate owned increased $112.1 million from December 31, 2007 to December 31, 2008. The increase was driven by deteriorating credit quality in the Company s loan portfolio. A substantial portion of the outstanding balance relates to properties in waterfront locations in Florida and coastal Alabama.

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Deposits

BancGroup s period end deposits consisted of the following:

	December 31,		% of Total	
	2008	2007	2008	2007
	(In thousands)			
Noninterest bearing demand deposits	**$ 2,816,699**	$ 2,988,457	**15.1%**	16.1%
Interest bearing demand deposits	**4,826,328**	6,307,491	**25.8**	34.0
Savings deposits	**346,880**	475,625	**1.9**	2.6
Non-time deposits	**7,989,907**	9,771,573	**42.8**	52.7
Certificates of deposit less than $100,000	**4,527,459**	3,566,220	**24.3**	19.2
Certificates of deposit $100,000 or more	**3,911,446**	3,143,193	**20.9**	16.9
Other time deposits	**678,483**	538,740	**3.6**	2.9
Retail deposits	**17,107,295**	17,019,726	**91.6**	91.7
Brokered time deposits	**1,297,651**	1,455,586	**7.0**	7.9
Reciprocal brokered time deposits	**268,319**	68,955	**1.4**	0.4
Total brokered time deposits	**1,565,970**	1,524,541	**8.4**	8.3
Total deposits	**$ 18,673,265**	$ 18,544,267	**100.0%**	100.0%

BancGroup continues to focus on growing deposits throughout its market areas. Total deposits increased 0.7% from December 31, 2007. The increase was driven by retail time deposits which increased $1.9 billion, or 25.8%, during 2008. This increase was substantially offset by a decrease in non-time deposit accounts of $1.8 billion, or 18.2%. Total brokered time deposits increased $41.4 million, or 2.7%, driven primarily by an increase of $199.3 million in reciprocal brokered time deposits which was partially offset by a reduction of $157.9 million in brokered time deposits from 2007 to 2008. In 2008, due to the current U.S. recession and its impact on the banking industry, reciprocal brokered time deposits became more attractive to customers looking to maximize FDIC insurance coverage. As market demographics change, products and services are restructured to meet the needs of a particular region or customer base. Refer to the *Liquidity and Funding* section of Management s Discussion and Analysis for further information.

The following chart details BancGroup s deposit base by state at December 31, 2008:

Total Deposit Base

At December 31, 2008, the scheduled maturities of time deposits in amounts of $100,000 or more were as follows:

Months to Maturity	(In thousands)
3 or less	$ 1,187,997
Over 3 through 6	799,447
Over 6 through 12	1,641,419
Over 12	512,445
Total	$ 4,141,308

Time deposit maturities of $9.4 billion in 2009 are expected to be renewed or substantially replaced by new originations. Over the past 12 months, 57.5% of total matured time deposits were renewed while new originations exceeded the level of maturing time deposits that did not renew. During January and February of 2009, $2.1 billion of time deposits matured and 49.7% of those deposits were renewed while Colonial increased total time deposits with $1.0 billion of new originations. If the level of time deposit renewals and originations is less than the level of maturities, Colonial could modify other deposit offerings or increase utilization of wholesale funding.

Short-Term Borrowings

Short-term borrowings consist of repurchase agreements, federal funds purchased and Federal Reserve Term Auction Facility (TAF) funds. Short-term borrowings increased $604 million, or 106%, from December 31, 2007 to December 31, 2008 as Colonial purchased $700 million in Federal Reserve TAF funds and decreased repurchase agreements by $96 million, or 17%. Refer to Note 16*, Short-Term Borrowings*, for additional information.

Long-Term Debt

Long-term debt consists of FHLB advances, subordinated debt, junior subordinated debt, and capital lease obligations. Total long-term debt increased $20 million, or 0.50%, from December 31, 2007 to December 31, 2008. During 2008, the Company issued $250 million in subordinated debt, which qualifies as Tier II regulatory capital; paid off $214 million in FHLB borrowings; and paid off $7.7 million of variable rate subordinated debt and $20.7 million of fixed rate subordinated debt. In addition, Colonial increased capital lease obligations by $3.4 million, or 22%. Refer to Note 17*, Long-Term Debt*, for additional information.

REIT Preferred Securities

During May 2007, the Company issued $300 million in fixed-to-floating rate perpetual non-cumulative preferred stock through its indirect subsidiary CBG Florida REIT Corp. When declared, dividends on these securities are payable at a rate of 7.114% until May 15, 2012 and at a rate of 3-month LIBOR plus 2.02% for each dividend period thereafter. CBG Florida REIT Corp., at its option and subject to certain restrictions, may redeem the preferred stock, in whole or in part, on May 15, 2012 and each fifth succeeding year thereafter. These securities qualify as Tier I capital. Refer to Note 20, *Minority Interest/REIT Preferred Securities*, for additional information.

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OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS

Off-Balance Sheet Arrangements

As a financial services provider, the Company routinely commits to extend credit, including loan commitments, letters of credit and financial guarantees. A significant portion of commitments to extend credit may expire without being drawn upon. These commitments are subject to the same credit policies and approval process used for loans. Also, in the ordinary course of business, the Company enters into indemnification agreements, including underwriting agreements relating to offers and sales of its securities, acquisition agreements and various other business arrangements, such as relationships arising from service as a director or officer of BancGroup or its subsidiaries. For more information regarding off-balance sheet arrangements, see Note 10, *Commitments and Contingent Liabilities*.

Contractual Obligations

The Company enters into contractual obligations in the ordinary course of business, including debt issuances for the funding of operations and leases for premises and equipment. The table below summarizes contractual obligations as of December 31, 2008 except for obligations of short-term borrowing arrangements and pension and postretirement benefits plans. More information on these obligations is contained in Note 16, *Short-Term Borrowings,* and Note 21, *Employee Benefit Plans*.

The Company also enters into derivatives, which create contractual obligations, as part of its interest rate risk management process. For more information, see the *Interest Rate Risk* section of Management s Discussion and Analysis and Note 12, *Derivatives*.

		Payments Due by Period				
Contractual Obligations	**Total**	**Less than 1 Year**	**1-3 Years**	**3-5 Years**	**After 5 Years**	**Other**
			(In thousands)			
Long-term debt par value(1)(2)	$ 4,095,908	$ 42,421	$ 99,388	$ 3,590	$ 3,950,509	$
Long-term debt interest(3)(4)	2,616,204	197,076	388,723	377,657	1,652,748	
Operating leases	411,195	40,442	75,786	54,491	240,476	
Time deposits	10,683,358	9,397,048	1,117,651	167,196	1,463	
Uncertain tax positions(5)	26,027					26,027
Total	$ 17,832,692	$ 9,676,987	$ 1,681,548	$ 602,934	$ 5,845,196	$ 26,027

(1) Excludes purchase accounting fair value adjustments, hedge accounting fair value adjustments and unamortized premiums and discounts.
(2) Includes principal payments related to capital leases totaling $18.5 million, payable as follows: $1.4 million in less than 1 year; $2.7 million in 1-3 years; $2.7 million in 3-5 years; and $11.7 million after 5 years.
(3) Includes interest payments related to capital leases totaling $9.3 million, payable as follows: $1.2 million in less than 1 year; $2.2 million in 1-3 years; $1.9 million in 3-5 years; and $4.0 million after 5 years.
(4) Includes interest on variable rate debt calculated using the effective contractual rates as of December 31, 2008.
(5) As of December 31, 2008, the Company had $26.0 million in uncertain tax positions. Due to the uncertainty of the timing of future cash flows associated with these obligations, reasonably reliable estimates of the periods of cash settlement with the respective taxing authorities cannot be made.

Time deposit maturities of $9.4 billion in 2009 are expected to be renewed or substantially replaced by new originations. Over the past 12 months, 57.5% of total matured time deposits were renewed while new originations exceeded the level of maturing time deposits that did not renew. During January and February of 2009, $2.1 billion of time deposits matured and 49.7% of those deposits were renewed while Colonial increased total time deposits with $1.0 billion of new originations. If the level of time deposit renewals and originations is less than the level of maturities, Colonial could modify other deposit offerings or increase utilization of wholesale funding. See the *Deposits* section of Management s Discussion and Analysis, and Note 15, *Time Deposits*, for additional information.

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RISK MANAGEMENT

Credit Risk Management

Colonial has some measure of credit risk in most of its primary banking activities, but the majority of this risk is associated with lending. The Company s credit risk management process is centered on credit and underwriting policies and procedures, a loan approval process that uses a committee structure, audit and review functions and credit professionals at the regional, business-line and BancGroup levels. In addition, Colonial has a credit risk reporting and analysis group which evaluates changes in credit risk, monitors large concentrations and exposures by types and locations and implements the Company s loan loss allowance methodology. Colonial also has a special assets/collections group which is charged with controlling losses, obtaining recoveries and implementing strategies to reduce problem asset levels. In addition, the internal auditors and regulatory examiners review and perform detailed tests of the Company s credit risk management activities, such as credit underwriting, loan administration and the loan loss allowance process. The overall goals of Colonial s credit risk management activities include providing an appropriate basis for new credit extensions and timely recognition of problems and risks.

In addition to lending, credit risk is present in Colonial s securities portfolio, derivative instruments and certain deposit activities. The Company s treasury and deposit departments have credit risk management processes in place in order to manage credit risk in these activities.

Loan Approval and Underwriting

The Chief Credit and Risk Officer, who reports directly to the Chief Executive Officer, provides company-wide credit oversight through a senior credit administration function. This function reviews larger credits prior to approval and also provides an independent review of credits on an ongoing basis. In addition, the Company has established regional loan committees comprised of local officers and directors that approve loans up to certain dollar amounts. These committees provide local business and market views while BancGroup s senior management provides oversight by participating in the state loan committees. Loans to the Company s largest borrowers and loans originated out of specialized business units may go through these committees for approval, but also are generally reviewed and approved by additional committees established by the Board of Directors and administered by the Chief Credit and Risk Officer.

Below is a summary of the most significant underwriting criteria used to evaluate new loans and loan renewals:

Cash flow and debt service coverage adequate cash flow is a necessary condition of credit worthiness. Loans not clearly supported by a borrower s cash flow must be justified by secondary repayment sources.

Secondary repayment sources alternative repayment funds significantly mitigate risk as long as the funds are liquid, easily accessible and adequate to supplement the primary cash flow source.

Underlying collateral value loans are generally secured by the asset being financed. However, unless it is liquid, it does not justify loans that cannot be serviced by the borrower s normal cash flows.

Overall credit worthiness of the customer the customer s relationships, both past and current, with both Colonial and other lenders are taken into account. Success depends on building lasting, mutually beneficial relationships with clients, which involves assessing their financial position and background.

Equity invested in the transaction in general, borrowers are required to contribute or invest a portion of their own funds prior to any loan advances.

Collateral guidelines vary with the type of loan and creditworthiness of the borrower, but generally require loan-to-value ratios ranging from 50% to 90%, depending on the loan type. Collateral values are monitored and estimated by loan officers and the senior credit administration function through inspections, independent appraisals, reference to broad measures of market values and current experience with similar properties or collateral.

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Commercial Real Estate and Real Estate Construction Loan Categories

A large portion of BancGroup s loans are secured by real estate, with commercial real estate and construction loans representing 33.9% and 33.8% of total loans as of December 31, 2008, respectively. BancGroup s commercial real estate and construction loans are spread geographically throughout Alabama, Florida and other areas including metropolitan Atlanta, Dallas, Reno and Las Vegas with no more than 12.5% of total commercial real estate and construction loans in any one metropolitan statistical area (MSA). The Alabama economy generally experiences a slow but steady rate of growth, while BancGroup s markets in Florida, Georgia, Nevada and Texas have historically experienced higher rates of growth. Currently, all of BancGroup s markets are experiencing a decline in real estate values due to an over supply of houses along with reduced demand for real estate, particularly residential real estate. The collateral held in the commercial real estate and construction portfolios consists of various property types such as retail properties, 1-4 family residential developments and lots, office buildings, land held for future development or construction, residential homes under construction, multi-family housing, condominium properties, warehouses, lodging and health service facilities. Colonial focuses its commercial real estate and construction lending efforts on properties owned and/or developed by experienced customers with whom BancGroup has established relationships. In addition to the subject properties, substantially all construction and commercial real estate loans have personal guarantees of the principals involved. The owner-occupied commercial real estate portfolio represented 34.0% of the total commercial real estate portfolio outstanding at December 31, 2008. Owner-occupied real estate is primarily dependent on cash flows from operating businesses rather than on the sale or rental of the property; therefore, these loans generally contain different inherent risks than other commercial real estate loans.

The following charts reflect the geographic diversity and property type distribution of total construction and commercial real estate loans at December 31, 2008:

	Construction	% of Total	Commercial Real Estate	% of Total
		(Dollars in thousands)		
Geographic Diversity (by property location)[1]				
Florida	$ 2,144,120	43.6%	$ 3,015,510	61.1%
Alabama	488,710	9.9%	543,261	11.0%
Georgia	511,470	10.4%	349,924	7.1%
Texas	947,705	19.2%	440,882	9.0%
Nevada	432,433	8.8%	199,693	4.0%
Other	397,752	8.1%	386,674	7.8%
Total	$ 4,922,190	100.0%	$ 4,935,944	100.0%

	Property Type Distribution % Construction Portfolio	Property Type Distribution % Total Portfolio		Property Type Distribution % Commercial Real Estate Portfolio	Property Type Distribution % Total Portfolio
Residential Construction			Retail	22.0%	7.5%
Residential development and lots	24.3%	8.2%	Office	21.5%	7.3%
Residential home construction	9.5%	3.2%	Warehouse	13.7%	4.6%
Residential land	7.0%	2.4%	Multi-Family	9.4%	3.2%
Condominium	5.5%	1.9%	Healthcare	9.1%	3.1%
Total Residential Construction	46.3%	15.7%	Lodging	6.2%	2.1%
Commercial Construction			Church or School	3.7%	1.3%
Commercial land	17.6%	6.0%	Industrial	2.5%	0.8%
Commercial development and lots	11.0%	3.7%	Farm	2.5%	0.8%
Retail	8.1%	2.7%	Other[2]	9.4%	3.2%
Multi-Family	3.9%	1.3%	**Total Commercial Real Estate**	100.0%	33.9%

Office	4.2%	1.4%
Other[2]	8.9%	3.0%
Total Commercial Construction	53.7%	18.1%
Total Construction	100.0%	33.8%

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(1) No more than 12.5% of construction and commercial real estate loans are in any one MSA.
(2) Other includes all loans in categories smaller than the lowest percentages shown above.

Selected Characteristics of the 75 Largest Construction and Commercial Real Estate Loans

	Construction	Commercial Real Estate
75 Largest Loans Total (in thousands)	$ 1,321,673	$ 1,001,470
% of 75 Largest Loans to Category Total	26.9%	20.3%
Average Loan to Value Ratio (75 largest loans)	73.2%	68.4%
Average Debt Coverage Ratio (75 largest loans)	N/A	1.51x

Residential Construction Loan Category

Residential construction represents approximately 46% of the Company s construction portfolio and consists of residential development and lots, residential home construction, residential land and condominiums. The loans are generally short-term, have the personal guarantees of the principals involved and are underwritten such that each borrower has substantial equity in the project.

The majority of the Company s nonperforming assets and net charge-offs during recent quarters relate to residential construction loans. The lack of real estate sales has caused liquidity issues for some of the Company s borrowers which have resulted in higher levels of nonperforming loans and losses in this portfolio.

The following table and chart show the components of residential construction loans, excluding nonperforming loans of approximately $300.4 million, at December 31, 2008:

Residential Construction Loans

	Total Outstanding Amount	%	Residential Development	Builder Lot Inventory	Consumer-Owned Lots	Residential Presold	Residential Speculative	Land	Condominium Construction
	(Dollars in millions)								
Florida	$ 885	45%	$ 309	$ 45	$ 65	$ 47	$ 109	$ 137	$ 173
Texas	483	24	303	23	5	12	42	84	14
Georgia	267	14	153	13	1	9	57	12	22
Alabama	227	11	71	22	24	17	62	25	6
Nevada	85	4	33	1		22	10	19	
Other	33	2	7	1	1	3	2	7	12
Total	$ 1,980	100%	$ 876	$ 105	$ 96	$ 110	$ 282	$ 284	$ 227

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Residential Construction Loans

Other Loan Categories

The risks associated with loans classified as commercial, financial and agricultural are generally related to the earnings capacity of, and the cash flows generated from, the specific business activities of the borrowers.

The risks associated with residential real estate loans are primarily related to the earnings capacity of the individual borrowers, as well as overall economic conditions which can adversely impact employment levels and property values. The Company has not offered any products targeting sub-prime borrowers and does not offer higher risk mortgage products such as option ARMs, pick a payment loans and low or no documentation loans.

Regarding consumer and other loans, the principal source of repayment is the earnings of the individual borrower and, on collateralized loans, the collateral serves as a secondary source of repayment.

Allowance for Loan Losses

Management s ongoing evaluation of the adequacy of the allowance for loan losses considers both impaired and unimpaired loans and takes into consideration Colonial s past loan loss experience, known and inherent risks in the portfolio, existing adverse situations that may affect the borrowers ability to repay, estimated value of any underlying collateral, an analysis of existing guarantees and an analysis of current economic conditions.

Colonial, through its lending and credit functions, performs ongoing reviews of its loan portfolio for credit risk. Colonial employs an independent credit review area that reviews the lending and credit functions to test the identification of credit risks. The Company remains committed to the timely recognition of problem loans and to ensuring an adequate level of allowance to cover inherent losses. Using information derived from the credit risk identification process, the Company s credit risk management area analyzes and performs the Company s allowance for loan losses calculations. The analysis includes four basic components: general allowances for loan pools, specific allowances for individual loans, allowances based on identified economic conditions and other risk factors and the overall allowance level (which gives rise to the unallocated component of the allowance).

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Management reviews the methodology, calculations and results and ensures that the calculations are appropriate and that all material risk elements have been assessed in order to determine the appropriate level of allowance for the inherent losses in the loan portfolio at each quarter end. Past due balances, nonaccrual balances, and potential problem loan balances are not absolute indicators of the losses inherent in the loan portfolio, but are considered in the overall evaluation of the adequacy of the allowance for loan losses. In addition, the allowance for loan losses methodology is discussed with, and reviewed by, the Risk Committee of the Board of Directors on a quarterly basis.

The following chart reflects the various tiers of reserves included in the allowance for loan losses:

Tier I	General allowance calculated based upon Colonial s historical losses
Tier II	Specific reserves for impaired loans
Tier III	Reserves for economic and other risk factors
Unallocated	Represents the imprecision inherent in the previous calculations
Total	Represents summation of all reserves

Tier I Reserves

The first reserve component (i.e. Tier I Reserves) is the general allowance for loan pools assessed by applying loss factors to groups of loans that have similar characteristics. This part of the methodology is governed by SFAS 5, *Accounting for Contingencies*. The general allowance factors are based upon recent and historical charge-off experience and are applied to the outstanding portfolio by loan type and internal risk rating. Historical loss analyses provide the basis for factors used for homogenous pools of smaller loans, such as residential real estate and other consumer loan categories which generally are not evaluated based on individual risk ratings but almost entirely based on historical losses. The statistics used in the Tier I analyses are adjusted quarterly based on loss trends and risk rating migrations.

As a result of the significant real estate market deterioration in the fourth quarter of 2007 and throughout 2008, the levels of classified and criticized loans, as well as net charge-offs, have increased. As a result the Tier I component of the Company s allowance for loan losses increased to $206.2 million at December 31, 2008, from $182.2 million at December 31, 2007

Tier II Reserves

The second component of the allowance (i.e. Tier II Reserves) involves the calculation of specific allowances for each impaired loan in accordance with SFAS 114, *Accounting by Creditors for Impairment of a Loan.* In situations where a loan is determined to be impaired (primarily because it is probable that all principal and interest amounts due according to the terms of the note will not be collected as scheduled), a specific reserve may or may not be warranted. Upon examination of the collateral and other factors, it may be determined that Colonial reasonably expects to collect all amounts due; therefore, no specific reserve is warranted. Any loan determined to be impaired (whether a specific reserve is assigned or not) is excluded from the Tier I calculations described above.

Colonial tests a broad group of loans for impairment each quarter (this includes all loans over $1 million that have internal risk ratings below a predetermined classification level, plus all loans over $500,000 that are more than 60 days past due). Once a loan is identified as impaired, reserves are based on a thorough analysis of the most probable source of repayment which is normally the liquidation of collateral, but may also include discounted future cash flows or the market value of the loan itself. Generally, for collateral dependent loans, current market appraisals are utilized for larger credits; however, in situations where a current market appraisal is not available, Colonial utilizes the best available information (including appraisals for similar properties, communications with qualified real estate professionals, information contained in reputable publications and other market data) to estimate the current fair value (less cost to sell) of the subject property. As a result of the increase in the level of impaired loans, the Tier II component of the allowance for loan losses increased to $48.6 million at December 31, 2008, from $11.0 million at December 31, 2007.

Tier III Reserves

The third component of the allowance (i.e. Tier III Reserves) represents the effect of risks or losses that are not fully captured elsewhere. This part of the allowance is calculated in accordance with SFAS 5 and reflects adjustments to historical loss experience to incorporate current economic conditions and other factors which impact the inherent losses contained in the portfolio. This component includes amounts for portfolio categories which are deemed to have risks not included in the other reserve elements as well as macroeconomic and other factors. The qualitative risk factors of this third allowance tier are more subjective and require a high degree of management judgment. Currently, the Tier III Reserves include additional reserves for Colonial s concentration in commercial real estate and construction loans as well as reserves for mortgage warehouse loans, and residential real estate loans. While the Tier III factors represent incremental risks inherent in the portfolio, due to the nature of the risks, the loss factors utilized in this component are not readily observable and therefore are based upon management s best estimation and are directionally consistent with current market conditions.

The Tier III Reserves for commercial real estate and construction are intended to provide for current elevated levels of economic risk as well as the inherent incremental risk resulting from Colonial s relative concentration in those loan types. The reserves for mortgage warehouse lending are included in Tier III because historical losses for this portfolio have been de minimis, and as such no Tier I reserve is calculated for this portfolio. The incremental reserves for residential mortgage loans are intended to represent the additional levels of inherent risk in this portfolio. As a result of the overall market deterioration during 2008 and the impact on the Company s asset quality metrics, the Tier III component of the allowance for loan losses increased to $55.4 million at December 31, 2008, from $28.6 million at December 31, 2007.

Unallocated Allowance

In addition to the Tier I, II and III reserves, unallocated reserves are included in the overall allowance for loan losses. The unallocated allowance is the result of management s judgment of risks inherent in the portfolio, economic uncertainties and other subjective factors, including industry trends, as well as the imprecision inherent in the estimates used for the allocated portions of the allowance. Management reviews the overall level of the allowance for loan losses as well as the unallocated component and considers the level of both amounts in determining the appropriate level of reserves to be maintained given the overall inherent risk in Colonial s total loan portfolio. The unallocated allowance totaled $14.7 million and $17.0 million at December 31, 2008 and 2007, respectively.

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Allocation of the Allowance for Loan Losses

	December 31,									
	2008		2007		2006		2005		2004	
	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans	Amount	Percent of Loans in Each Category to Total Loans
	(Dollars in thousands)									
Balance at end of period applicable to:										
Commercial, financial and agricultural	**$ 50,859**	**11.8%**	$ 44,425	9.5%	$ 42,148	9.3%	$ 44,244	10.6%	$ 47,404	16.5%
Commercial real estate	**66,859**	**33.9%**	28,678	31.4%	26,820	27.7%	40,311	29.7%	37,393	33.2%
Real estate construction	**157,576**	**33.8%**	119,723	39.5%	64,487	40.9%	41,826	36.8%	30,357	30.5%
Residential real estate	**24,947**	**17.7%**	16,702	16.8%	18,337	19.3%	20,734	20.4%	12,494	17.3%
Consumer and other	**10,070**	**2.8%**	12,328	2.8%	11,265	2.8%	10,030	2.5%	9,075	2.5%
Unallocated	**14,689**	**NA**	16,989	NA	11,793	NA	13,906	NA	12,079	NA
Total	**$ 325,000**	**100.0%**	$ 238,845	100.0%	$ 174,850	100.0%	$ 171,051	100.0%	$ 148,802	100.0%
Percent of Reserve to Loan Category										
Commercial, financial and agricultural	**2.97%**		2.95%		2.93%		2.78%		2.23%	
Commercial real estate	**1.35%**		0.57%		0.62%		0.91%		0.88%	
Real estate construction	**3.20%**		1.90%		1.02%		0.76%		0.77%	
Residential real estate	**0.97%**		0.62%		0.61%		0.68%		0.56%	
Consumer and other	**2.50%**		2.72%		2.57%		2.69%		2.88%	
Unallocated	**NA**		NA		NA		NA		NA	
Total	**2.24%**		1.50%		1.13%		1.15%		1.16%	

The following table summarizes changes in the balance of the allowance for loan losses as well as loan loss experience:

	Year Ended December 31,				
	2008	2007	2006	2005	2004
	(Dollars in thousands)				
Balance January 1	**$ 238,845**	$ 174,850	$ 171,051	$ 148,802	$ 138,549
Additions due to acquisitions		13,914		14,622	6,857
Provision charged to income	**728,942**	106,450	22,142	26,838	26,994
Reduction due to sale of mortgage loans originally held for investment		(2,303)			
Loans charged off	**(647,933)**	(61,338)	(30,779)	(27,206)	(29,811)
Recoveries	**5,146**	7,272	12,436	7,995	6,213
Balance December 31	**$ 325,000**	$ 238,845	$ 174,850	$ 171,051	$ 148,802
Loans (net of unearned income) December 31	**$ 14,530,018**	$ 15,923,178	$ 15,478,889	$ 14,899,864	$ 12,857,811
Ratio of ending allowance to ending loans (net of unearned income)	**2.24%**	1.50%	1.13%	1.15%	1.16%
Average loans (net of unearned income)	**$ 15,454,146**	$ 15,290,766	$ 15,339,699	$ 14,139,380	$ 12,148,513
Ratio of net charge-offs to average loans (net of unearned income)	**4.16%**	0.35%	0.12%	0.14%	0.19%

BancGroup also maintains a reserve against certain unfunded commitments, including letters of credit. This reserve is included in other liabilities and totaled $3.0 million and $1.0 million as of December 31, 2008 and 2007, respectively.

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Analysis of Net Charge-Offs

	December 31,				
	2008	**2007**	**2006**	**2005**	**2004**
	(Dollars in thousands)				
Charge-offs:					
Commercial, financial and agricultural	**$ 34,669**	$ 4,034	$ 17,346	$ 8,452	$ 10,854
Commercial real estate	**47,843**	3,648	1,537	8,860	8,034
Real estate construction	**527,307**	45,363	5,690	2,445	2,670
Residential real estate	**25,909**	4,214	1,702	3,155	2,613
Consumer and other	**12,205**	4,079	4,504	4,294	5,640
Total charge-offs	**647,933**	61,338	30,779	27,206	29,811
Recoveries:					
Commercial, financial and agricultural	**1,733**	4,386	5,914	3,546	2,855
Commercial real estate	**245**	118	3,175	1,171	776
Real estate construction	**839**	410	571	254	223
Residential real estate	**531**	560	428	584	480
Consumer and other	**1,798**	1,798	2,348	2,440	1,879
Total recoveries	**5,146**	7,272	12,436	7,995	6,213
Net charge-offs:					
Commercial, financial and agricultural	**32,936**	(352)	11,432	4,906	7,999
Commercial real estate	**47,598**	3,530	(1,638)	7,689	7,258
Real estate construction	**526,468**	44,953	5,119	2,191	2,447
Residential real estate	**25,378**	3,654	1,274	2,571	2,133
Consumer and other	**10,407**	2,281	2,156	1,854	3,761
Total net charge-offs	**$ 642,787**	$ 54,066	$ 18,343	$ 19,211	$ 23,598
Percent of net charge-offs to average loan category:					
Commercial, financial and agricultural	**2.07%**	(0.03)%	0.78%	0.28%	0.41%
Commercial real estate	**0.95%**	0.08%	(0.04)%	0.17%	0.17%
Real estate construction	**9.11%**	0.71%	0.09%	0.05%	0.07%
Residential real estate	**0.97%**	0.13%	0.04%	0.09%	0.10%
Consumer and other	**2.29%**	0.47%	0.49%	0.51%	1.14%
Total	**4.15%**	0.35%	0.12%	0.14%	0.19%

While the majority of 2008 net charge-offs occurred in the Company s real estate construction portfolio, the other components of the loan portfolio also experienced elevated levels of charge-offs arising from the current U.S. recession.

Nonperforming Assets and Potential Problem Loans

Colonial maintains an active nonaccrual and problem loan identification program. Through the ongoing monitoring and review of the various risks in the loan portfolio, this program aids in the timely identification of problem loans and the minimization of the risk of loss.

Nonperforming assets consist of loans on nonaccrual status, renegotiated loans, other real estate owned, repossessions and loans held for sale on nonaccrual status. Loans are generally placed on nonaccrual status if full collection of principal and interest becomes unlikely (even if all payments are current) or if the loan is delinquent in principal or interest payments for 90 days or more, unless the loan is well secured and in the process of collection. BancGroup s policy is to charge-off consumer installment loans when they become 120 days past due unless they are in the process of foreclosure and are adequately collateralized. Management monitors all loans that are contractually 90 days past due, renegotiated or nonaccrual.

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Other real estate owned includes real estate acquired through foreclosure or by deed taken in lieu of foreclosure. These properties are recorded at estimated fair value, less costs to sell, with any initial difference between the fair value of the property and the carrying value of the loan being charged to the allowance for loan losses. Subsequent changes in fair value are reported as adjustments to the carrying amount, not to exceed the adjusted carrying value of the assets at the time of transfer. Those subsequent changes, as well as any gains or losses recognized on the sale of these properties, are included in noninterest expense.

Nonperforming Assets

	December 31, 2008	2007	2006	2005	2004
	(Dollars in thousands)				
Nonaccrual loans:					
Commercial, financial and agricultural	**$ 14,750**	$ 2,467	$ 1,887	$ 4,582	$ 10,033
Commercial real estate	**48,508**	6,374	5,904	15,088	12,447
Real estate construction	**394,324**	96,397	1,504	2,143	1,026
Residential real estate	**74,186**	15,993	3,987	3,385	3,018
Consumer and other	**998**	655	743	470	459
Total nonaccrual loans*	**532,766**	121,886	14,025	25,668	26,983
Aggregate loans renegotiated to provide a reduction or deferral of interest or principal because of deterioration in the financial condition of the borrower (not included above)	**586**			155	191
Total nonperforming loans*	**533,352**	121,886	14,025	25,823	27,174
Other real estate owned	**127,850**	15,760	1,850	6,032	9,711
Repossessions	**58**		19	76	154
Nonaccrual loans transferred to held for sale	**49,198**		9,255		
Total nonperforming assets*	**$ 710,458**	$ 137,646	$ 25,149	$ 31,931	$ 37,039
Aggregate loans contractually past due 90 days or more for which interest is being accrued	**$ 41,579**	$ 23,837	$ 8,138	$ 10,283	$ 8,096
Net charge-offs year-to-date	**$ 642,787**	$ 54,066	$ 18,343	$ 19,211	$ 23,598
Total nonperforming loans as a percent of loans, net of unearned income	**3.67%**	0.77%	0.09%	0.17%	0.21%
Total nonperforming assets* as a percent of loans, net of unearned income, other real estate owned, repossessions and nonaccrual loans transferred to held for sale	**4.83%**	0.86%	0.16%	0.21%	0.29%
Total nonperforming loans and 90 day past due loans for which interest is being accrued as a percent of loans, net of unearned income	**3.96%**	0.92%	0.14%	0.24%	0.27%
Allowance as a percent of loans, net of unearned income	**2.24%**	1.50%	1.13%	1.15%	1.16%
Allowance as a percent of nonperforming loans*	**61%**	196%	1247%	662%	548%

* Does not include loans contractually past due 90 days or more which are still accruing interest.

The balance of nonperforming assets can fluctuate due to changes in economic conditions, nonperforming assets obtained in acquisitions and the disproportionate impact of larger assets. The increase in nonperforming assets in 2008 was primarily caused by a decline in the value of residential real estate which negatively impacted the liquidity of a number of borrowers. Refer to the *Allowance for Loan Losses* discussion in the *Risk Management* section of Management s Discussion and Analysis for additional information.

For loans classified as nonperforming as of December 31, 2008, the gross interest income that would have been recorded in 2008 if the loans had been current in accordance with their original terms for the period they were outstanding during the year, was $49.6 million. The amount of interest income on those loans that was included in pretax net income in 2008 was $27.5 million.

During 2008, the Company modified the terms of certain loans to accommodate the borrowers deteriorated financial condition. These loans, which had an outstanding principal balance of $18.5 million, were charged-down by $11.0 million. As of December 31, 2008, $586,000 of these loans were accruing interest. As of December 31, 2008, the Company had no commitments to lend additional funds to these borrowers.

Impaired loans totaled $462.3 million and $105.4 million at December 31, 2008, and December 31, 2007, respectively. The related allowance for loan losses on impaired loans was $48.6 million at December 31, 2008 compared with $11.0 million at December 31, 2007. Impaired loans at December 31, 2008 were previously charged down by $161.5 million. Substantially all of the impaired loans were on nonaccrual status, and as such were included in nonperforming assets.

In addition to nonperforming assets, the Company is aware of a number of potential problem loans where possible credit problems of borrowers cause management to have concerns as to the ability of such borrowers to comply with present loan repayment terms and which may result in these loans being classified as nonperforming in the future. There were $695.6 million of potential problem loans identified at December 31, 2008 compared to $702.8 million at December 31, 2007. Although these loans have been identified as potential problem loans, they may never become delinquent, nonperforming or impaired. Potential problem loans are considered in the determination of the adequacy of the allowance for loan losses.

As noted in the preceding data, a significant portion of the Company s loan losses and nonperforming loans have been concentrated in the real estate construction loan portfolio; whereas the commercial real estate portfolio has been less impacted. If market conditions deteriorate further, thereby placing increased pressure on the commercial real estate market, Colonial s commercial real estate loan portfolio quality could be adversely impacted, thereby resulting in additional loan losses.

Asset/Liability Management

Asset/liability management (ALM) involves the evaluation, monitoring and management of interest rate risk, liquidity and funding. The Board of Directors has overall responsibility for Colonial s ALM policies. To ensure adherence to these policies, the Risk Committee of the Board of Directors and the Asset Liability Management Committee (ALMCO) establish and monitor guidelines to control the sensitivity of earnings to changes in interest rates. ALMCO is comprised of senior members of management and meets periodically to oversee the implementation of the ALM policies. The ALM guidelines apply to both on- and off-balance sheet positions. The goal of ALM is to maximize earnings while carefully controlling interest rate risk.

Interest Rate Risk

The majority of the Company s assets and liabilities are monetary in nature. Therefore, interest rate risk, and its potential effect on earnings, is the most significant market risk exposure inherent in our operations. BancGroup is subject to interest rate risk because:

- Assets and liabilities may mature or re-price at different times (for example, if assets re-price faster than liabilities and interest rates are generally falling, earnings will initially decline).

- Assets and liabilities may re-price at the same time but by different magnitudes or velocities (for example, when the general level of interest rates is falling, Colonial Bank may reduce rates paid on checking and savings deposit accounts by an amount that is less than the general decline in market interest rates).

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Assets and liabilities may reprice at the same time, but in response to different market factors or indices (for example, even if equal amounts of assets and liabilities reprice at the same time, some may reprice with higher rates and others with lower rates).

Short-term and long-term market interest rates may change by different amounts or in different directions (for example, the shape of the yield curve may affect new loan yields and funding costs differently).

Assets and liabilities may contain option risk whereby the counterparty can take advantage of changes in interest rates without penalty (for example, when interest rates decline, loan customers may prepay fixed rate loans by refinancing at a lower rate which could reduce interest income).

The remaining maturity of various assets or liabilities may shorten or lengthen as interest rates change (for example, if long-term mortgage interest rates decline sharply, mortgage-backed securities held in the securities available for sale portfolio may prepay significantly earlier than previously anticipated which could reduce portfolio income).

Factors other than market interest rates, such as economic conditions, customer preferences for specific products, and the competitive environment within Colonial s markets, can also impact interest rate risk.

Interest rate levels may have an indirect impact on loan demand, credit losses, mortgage origination volume, the value of BancGroup s pension asset/liability and other sources of earnings.

ALM activities include lending, accepting and placing deposits, investing in securities, maintenance of cash and balances due from banks and the Federal Reserve, issuing debt and hedging interest rate risk. Sensitivity of earnings to interest rate changes arises when yields on assets change in a different time period or in a different amount from interest cost on liabilities. To mitigate interest rate risk, the structure of the balance sheet is managed so that movements of interest rates on assets and liabilities are projected to be correlated in a manner intended to allow Colonial s interest bearing assets and liabilities to contribute to earnings even in periods of volatile interest rates.

Colonial employs simulations of net interest income and the economic value of equity as measurement techniques in the management of interest rate risk. The simulation of net interest income measures the expected changes in income in response to changes in interest rates, while the economic value of equity measures the expected change in the fair value of equity arising from the changes in the fair value of Colonial s assets and liabilities in response to changes in interest rates. These techniques are complementary and are used in concert to provide a comprehensive interest rate risk management capability. Actual results may differ significantly from those derived using these modeling techniques due to the timing, magnitude and frequency of interest rate changes, actual management responses to those changes, changes in customer behavior, and the possible effects of unanticipated or unknown events.

Simulation of earnings is the primary tool used to measure the sensitivity of earnings to interest rate changes. Using computer modeling techniques, Colonial is able to measure the potential impact of different interest rate assumptions on net interest income. All balance sheet positions, including derivative financial instruments, are included in the model simulation.

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The table below presents the output from the Company s simulation model based on Colonial s balance sheet at December 31, 2008, with comparable prior year information. The table measures, consistently for both years, the impact on net interest income of an immediate and sustained change in all market interest rates in 100 basis point increments for the twelve calendar months following the date of the change. This twelve-month projection of net interest income under these scenarios is compared to the twelve-month net interest income projection with rates unchanged.

Basis Points Change:	Federal Funds Rate December 31,		Percentage Change in 12 Month Projected Net Interest Income Versus Projected Net Interest Income Under No Rate Change(1) December 31,	
	2008	2007	2008	2007
+200	**2.25**	6.25	**(1.1)%**	3.0%
+100	**1.25**	5.25	**(0.5)%**	2.1%
No rate change	**0.25**	4.25		
100	**NM**	3.25	**NM**	(2.0)%
200	**NM**	2.25	**NM**	(4.2)%

(1) The computation of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of different market interest rates, estimates of rates on loans and deposits given these rate changes, the ability to maintain interest rate floors on loans and other assets as market rates decline, deposit decay rates and asset prepayment rates. Further, the computations do not take into account changes to the slope of the yield curve, changes in the relative relationship of various market rates, or changes in the volume or mix of assets and liabilities on the balance sheet nor do they contemplate any actions BancGroup could undertake in response to these changes in interest rates.

NM Not meaningful

As shown in the table above, the Company s balance sheet became somewhat liability sensitive through the +200 basis points scenario at December 31, 2008 whereas it was asset sensitive at December 31, 2007. On the asset side, an increase in the proportion of variable rate assets due to a large increase in the Company s interest bearing deposits in banks and the Federal Reserve increased asset sensitivity. Liabilities have become less sensitive to changes in interest rates due to a shift from non-term transaction accounts to longer term time deposits as well as a shift from variable FHLB and long-term debt to fixed rate products as FHLB advances converted to fixed rates and a $210 million fixed to variable interest rate swap on subordinated debt that was terminated because of default by the counterparty. Due to the significant decline in market rates of approximately 400 basis points in the base scenario, the rate floors on approximately $4.3 billion of mortgage warehouse assets are currently in the money and therefore provide for a shift to liability sensitivity in the increasing rate scenarios. The rate floors do not reprice until a market rate increase of over 200 basis points.

Colonial also measures interest rate risk by simulating the impact of changes in interest rates on the market value of equity. The potential effect of these interest rate changes is derived from the collective impact of such changes on the market value of assets and liabilities. This analysis is highly dependent upon assumptions applied to assets and liabilities with noncontractual maturities. These assumptions are based on historical behaviors and management estimates. Colonial analyzes the changes in market value of equity to ensure that the Company maintains an adequate capital and ALM position.

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The table below presents the output of the simulation model for the economic value of equity (EVE), which is defined as the net present value of interest rate sensitive assets, interest rate sensitive liabilities and off-balance sheet contracts. The table represents the percentage change in the EVE under 100 basis point parallel rate shocks versus the EVE assuming rates at December 31, 2008 and 2007.

Basis Points Change:	Federal Funds Rate December 31, 2008	2007	Percentage Change in EVE vs. EVE Under No Rate Change December 31, 2008	2007
+200	**2.25**	6.25	**10.7%**	(6.2)%
+100	**1.25**	5.25	**7.9%**	(1.7)%
No rate change	**0.25**	4.25		
100	**NM**	3.25	**NM**	(3.3)%
200	**NM**	2.25	**NM**	(13.1)%

NM Not meaningful.

Liquidity and Funding

Liquidity is the ongoing ability of an organization to meet its financial commitments and obligations on a timely basis and without adverse consequences. These commitments and obligations include credit needs of customers, withdrawals by depositors, repayment of borrowings when due and payment of operating expenses, interest and dividends. Management of liquidity also includes management of funding sources and their utilization based on current, future and contingency needs. Maintaining and managing adequate liquidity and funding are other prominent focuses of ALM.

The Company s liquidity can be adversely affected by both direct and indirect circumstances. For example, a direct event could be deterioration in the public perception of the Company leading to higher borrowing and/or deposit cost or declining availability thereof. Indirect events that could affect Colonial would be a U.S. capital market collapse, terrorism, war, natural disasters, political events or significant deterioration in the perception of financial institutions in general.

Liquidity is also important for the parent company on a standalone basis to ensure that sufficient funds are available to meet all obligations of the parent company as they become due. The parent company s cash requirements typically consist of debt service, investments in and advances to subsidiaries, operating expenses, income taxes, any dividends to shareholders and any share repurchases. At December 31, 2008, the parent company held deposits in Colonial Bank totaling $99.9 million and maintained an investment portfolio of $21.7 million. Collectively these amounts exceed the parent company s expected debt service and cash operating expenses for 2009 and 2010. The parent company has previously issued long-term debt as a source of liquidity. As discussed under *Regulatory Restrictions*, the ability of Colonial Bank to dividend, lend or otherwise provide funds to the parent company is limited by federal and state banking regulations. Additionally, as discussed under *Payment of Dividends and Other Restrictions* in Item 1, both Colonial Bank and BancGroup are required to receive prior regulatory approval for the payment of dividends on common stock.

Deposit growth remains a primary focus of the Company s funding and liquidity strategy. Colonial s period end deposits grew by $129.0 million, or 1%, from December 31, 2007 and retail deposits increased an annualized 11% during the fourth quarter of 2008. Retail deposits have been, and are expected to continue to be, the primary component of BancGroup s funding base. However, during 2008, intense competition for retail deposits increased the cost of deposits above certain wholesale sources. Time deposit maturities of $9.4 billion in 2009 are expected to be renewed or substantially replaced by new originations. Over the past 12 months, 57.5% of total matured time deposits were renewed while new originations exceeded the level of maturing time deposits that did not renew. During January and February of 2009, $2.1 billion of time deposits matured and 49.7% of those deposits were renewed while Colonial increased total time deposits with $1.0 billion of new originations. If the level of time deposit renewals and originations is less than the level of maturities, Colonial could modify other deposit offerings or increase utilization of wholesale funding. See the *Deposits* section of Management s Discussion and Analysis, and Note 15, *Time Deposits*, for additional information.

At December 31, 2008, the Company had estimated available wholesale funding in excess of $5.4 billion. BancGroup has worked to maintain the availability of short-term and long-term wholesale funding sources to complement its retail deposit base. The Company has drawn on a variety of funding sources to assist in funding earning assets and managing deposit fluctuations. Colonial has utilized Federal Funds lines, collateralized funding facilities and brokered time deposits as sources for short-term borrowings. The FHLB is also an important source of wholesale funding for BancGroup. As of December 31, 2008, the lendable collateral value pledged to the FHLB amounted to $3.5 billion. To provide both capital and long-term funding, BancGroup has previously issued REIT preferred securities, subordinated debentures, subordinated notes, junior subordinated debt and common stock and has utilized brokered time deposits. During 2009, only $42.4 million of BancGroup s long term debt will mature. See the *Short-Term Borrowings* and *Long-Term Debt* sections of Management s Discussion and Analysis, and Note 16, *Short-Term Borrowings*, and Note 17, *Long-Term Debt*, for additional information.

In response to the significant market and economic uncertainty in the United States, and particularly in portions of Colonial s geographic footprint, Colonial maintained cash and interest bearing deposits in banks and the Federal Reserve of over $2.0 billion at December 31, 2008, up from $504 million in the prior year. As of December 31, 2008, Colonial held $1.1 billion at the Federal Reserve and $388.5 million at the FHLB of Atlanta.

Colonial has approximately $3.5 billion in outstanding securities, most of which are debt securities. Approximately 96.1% of these securities are either government sponsored or have an investment grade rating. Securities totaling approximately $1.8 million will mature in 2009. See the *Securities* section of Management s Discussion and Analysis, and Note 6, *Securities*, for additional information.

Short-term borrowings were comprised of the following at December 31, 2008, 2007 and 2006:

	2008	**2007**	**2006**
		(In thousands)	
Federal funds purchased	**$**	$	$ 1,133,000
Federal Reserve TAF	**700,000**		
Repurchase agreements (retail)	**472,706**	568,721	532,672
Repurchase agreements (wholesale)			300,000
Total short-term borrowings	**$ 1,172,706**	$ 568,721	$ 1,965,672

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Additional details regarding short-term borrowings are shown below:

	Maximum Outstanding At Any Month End	Average Balance	Average Interest Rate	Average Interest Rate At December 31
		(Dollars in thousands)		
2008				
Federal funds purchased	**$ 1,555,000**	**$ 386,962**	**3.00%**	**NA**
Federal Reserve TAF	**700.000**	**160,656**	**1.39%**	**1.39%**
Other short-term borrowings	**1,096,479**	**633,015**	**2.82%**	**1.06%**
	$ 3,351,479	**$ 1,180,633**	**2.58%**	**1.26%**
2007				
Federal funds purchased	$ 1,051,500	$ 645,686	5.14%	NA
Other short-term borrowings	1,172,017	801,343	4.34%	3.40%
	$ 2,223,517	$ 1,447,029	4.69%	3.40%
2006				
FHLB borrowings	$ 250,000	$ 39,315	5.42%	NA
Federal funds purchased	1,628,400	1,079,743	5.12%	5.24%
Other short-term borrowings	948,327	867,645	4.30%	4.51%
	$ 2,826,727	$ 1,986,703	4.77%	4.93%

Long-term debt was comprised of the following at December 31, 2008, 2007 and 2006:

	2008	2007	2006
		(In thousands)	
Variable rate subordinated debentures	**$**	$ 7,725	$ 7,725
Subordinated notes(1)	**615,336**	378,709	376,114
Junior subordinated debt	**108,248**	108,256	299,078
FHLB borrowings(1)	**3,301,722**	3,513,997	1,835,228
Capital lease obligations	**18,501**	15,149	4,128
Total long-term debt	**$ 4,043,807**	$ 4,023,836	$ 2,522,273

(1) Includes an adjustment to fair market value as required by SFAS 133, due to related interest rate swaps. See Note 12, *Derivatives*, and Note 17, *Long-Term Debt*, for further details.

During 2008, the Company issued $250 million of 8.875% subordinated notes due March 15, 2038. The notes qualify as Tier II regulatory capital for BancGroup. Colonial may redeem the notes in whole or in part on or after March 15, 2013 in accordance with Federal Reserve guidelines.

During 2008, the Company completed a public common stock offering of 43.7 million shares at $8.00 per share for $350 million. The Company incurred approximately $16 million of offering expenses which were netted against the proceeds. See Note 18, *Capital Stock*, for additional information.

During 2007, the Company issued $300 million in fixed-to-floating rate perpetual non-cumulative preferred stock that pays dividends at an initial rate of 7.114%. See Note 20, *Minority Interest/REIT Preferred Securities*, for additional information.

The Company s significant contractual obligations and commitments are presented within the *Off-Balance Sheet Arrangements and Contractual Obligations* section of Management s Discussion and Analysis. The Consolidated Statements of Cash Flows summarize the Company s sources and uses of cash by type of activity for each of the three years in the period ended December 31, 2008.

Operational Risk Management

In providing banking services, Colonial processes cash, checks, wires and ACH transactions which expose Colonial to operational risk. Controls over such processing activities are monitored to safeguard the assets of Colonial and its customers. However, from time to time, Colonial has incurred losses related to these processes, and there can be no assurance that such losses will not occur in the future.

Operational risk is the risk of unexpected losses attributable to human error, systems failures, fraud or inadequate internal controls and procedures. This risk is mitigated through a system of internal controls that are designed to keep operational risk at levels appropriate to Colonial s corporate standards in view of the risks inherent in the markets in which Colonial operates. The system of internal controls includes policies and procedures that require the proper authorization, approval, documentation and monitoring of transactions. Each business unit is responsible for complying with corporate policies and procedures. Colonial s internal auditors monitor the overall effectiveness of the system of internal controls on an ongoing basis.

Colonial attempts to avoid engaging in business processes that are out of its primary areas of expertise. Instead, Colonial outsources certain non-core processing functions to limit operational risk associated with non-core activities.

Operational losses are monitored closely and have historically been absorbed by current earnings without any material impact to earnings or capital.

CAPITAL MANAGEMENT

Capital Adequacy and Resources

Management is committed to maintaining capital at a level sufficient to protect shareholders and depositors, provide for reasonable growth and fully comply with all regulatory requirements. Management s strategy to achieve these goals is to suspend payment of dividends on common stock and to increase capital through one or more strategies, including the pursuit of private equity investors to facilitate the satisfaction of the capital raising condition for the Company to issue all or a portion of the allowable TARP preferred stock.

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The Federal Reserve Board has issued guidelines identifying minimum Tier I leverage ratios relative to total assets and minimum capital ratios relative to risk-adjusted assets. Generally, the minimum leverage ratio required for a bank holding company is 4%. The minimum risk-based capital ratios established by the Federal Reserve are 4% for Tier I and 8% for total capital. Higher capital ratios may be required by the Federal Reserve if warranted by the circumstance or risk profile. BancGroup and Colonial Bank s actual capital ratios and BancGroup s components of capital and risk adjusted asset information (subject to regulatory review) are stated below:

	December 31, 2008	December 31, 2007
	(Dollars in thousands)	
BancGroup s Risk-Based Capital:		
Shareholders equity	**$ 1,344,978**	$ 2,273,571
Unrealized losses on securities available-for-sale	**310,015**	3,673
Net impact of actuarial losses/gains and cash flow hedges	**12,375**	741
Qualifying minority interests in consolidated subsidiaries	**293,373**	293,812
Qualifying trust preferred securities	**105,000**	105,000
Intangible assets (net of allowed deferred taxes)	**(466,222)**	(1,053,822)
Disallowed deferred tax assets	**(63,715)**	
Other adjustments	**(986)**	(3,304)
Tier I Capital	**1,534,818**	1,619,671
Allowable loan loss and unfunded commitment reserves	**224,955**	239,845
Subordinated debt	**544,679**	310,805
45% of net unrealized gains on equity securities available-for-sale	**5**	
Tier II Capital	**769,639**	550,650
Total Capital	**$ 2,304,457**	$ 2,170,321
Risk-Adjusted Assets	**$ 17,893,357**	$ 19,715,951
Quarterly Average Assets (for regulatory purposes)	**$ 26,006,943**	$ 24,266,011
BancGroup s Capital Ratios:		
Tier I Leverage Ratio	**5.90%**	6.67%
Risk-Adjusted Capital Ratios:		
Tier I Capital Ratio	**8.58%**	8.22%
Total Capital Ratio	**12.88%**	11.01%
Colonial Bank s Capital Ratios:		
Tier I Leverage Ratio	**6.03%**	6.32%
Risk-Adjusted Capital Ratios:		
Tier I Capital Ratio	**8.54%**	7.77%
Total Capital Ratio	**11.37%**	10.56%

Common Stock Offering

On April 25, 2008, the Company completed a public common stock offering of 43.7 million shares at $8.00 per share for $350 million. The Company received proceeds of $334.2 million, which was net of all expenses, commissions and underwriters discounts. The Company used the proceeds for general corporate purposes as well as investments in subsidiaries.

Regulatory Restrictions

Due to their current condition and results of operations, BancGroup and Colonial Bank are operating under heightened regulatory scrutiny and have been and will be taking steps to improve their asset quality and capital. For further information, see the discussion in *Risk Factors* in Item 1A and Note 19, *Regulatory Matters and Restrictions*. These matters are a major focus of the attention and efforts of the Board of Directors and management.

Colonial Bank is also required to maintain reserve balances with the Federal Reserve Bank based on a percentage of deposits reduced by its cash on hand. The average amounts of the required reserves were approximately $24.2 million and $6.5 million for the years ended December 31, 2008 and 2007, respectively.

Replacement Capital Covenant

In connection with the issuance of the REIT Preferred Securities, BancGroup entered into a Replacement Capital Covenant (RCC). The RCC was executed by BancGroup in favor of the holders of Colonial Bank s 6.375% subordinated notes issued December 7, 2005. Under the RCC and in the event of the prepayment, redemption, or repurchase of the REIT Preferred Securities prior to May 15, 2017, BancGroup has agreed to issue replacement qualified capital securities meeting certain minimum criteria. The RCC is more fully described in the Current Report on Form 8-K filed May 29, 2007.

RECENT ACCOUNTING STANDARDS

Standards adopted in 2008

In September 2008, the FASB issued FSP FAS 133-1 and FIN 45-4, *Disclosures about Credit Derivatives and Certain Guarantees: An Amendment of FASB Statement No. 133 and FASB Interpretation No. 45; and Clarification of the Effective Date of FASB Statement No. 161.* This FSP amends SFAS 133 to require a seller of credit derivatives, including credit derivatives embedded in hybrid instruments, to disclose for each statement of financial position presented: the nature of the credit derivative; the maximum potential amount of future undiscounted payments the seller could be required to make under the credit derivative contract (or the fact that there is no limit to the maximum potential future payments); the fair value of the derivative; and the nature of any recourse provisions and assets held as collateral or by third parties that the seller can obtain and liquidate to recover all or a portion of the amounts paid under the credit derivative contract. These disclosures must be provided even if the likelihood of having to make payments is remote. In addition, this FSP amends FIN 45, *Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness to Others,* to require guarantors to disclose the current status of the payment/performance risk of a guarantee. The provisions of this FSP that amend SFAS 133 and FIN 45 are effective for annual or interim reporting periods ending after November 15, 2008. This FSP also clarifies that SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. Because FSP FAS 133-1 and FIN 45-4 only requires additional disclosures, the adoption of the standard did not impact the Company s financial condition, results of operations or cash flows. The Company does not sell credit derivatives; therefore, the portion of the standard that requires additional disclosures by sellers of credit derivatives is not applicable to Colonial. The Company does have standby letters of credit which are considered guarantees that are in the scope of FIN 45. See Note 10, *Commitments and Contingent Liabilities,* for disclosure regarding the current status of the payment/performance risk of the Company s standby letters of credit.

In September 2008, the SEC Office of the Chief Accountant and the FASB Staff jointly issued Release 2008-234, *SEC Office of the Chief Accountant and FASB Staff Clarifications on Fair Value Accounting*. Release 2008-234 provides general clarification guidance on determining fair value under SFAS 157 when markets are inactive. On October 10, 2008, the FASB Staff issued FSP FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active,* which includes guidance that is consistent with Release 2008-234. FSP FAS 157-3 amends SFAS 157 by incorporating an example to illustrate key considerations in determining the fair value of a financial asset in an inactive market. With regard to the measurement principles of SFAS 157, this FSP reaffirms the notion of fair value as an exit price as of the measurement date. Additionally, this FSP provides clarification on how management s internal cash flow and discount rate assumptions should be considered when measuring fair value when relevant observable data does not exist, how observable market information in a market that is not active should be considered when measuring fair value, and how the use of market quotes (for example, broker quotes or pricing services for the same or similar financial assets) should be considered when assessing the relevance of observable and unobservable data available to measure fair value. This FSP became effective upon issuance. BancGroup applied the guidance in Release 2008-234 and FSP FAS 157-3 when determining fair value for the Company s non-agency mortgage-backed securities as of December 31, 2008. See Note 5*, Fair Value Measurements*, for further discussion.

In December 2008, the FASB issued FSP FAS 140-4 and FIN 46(R)-8, *Disclosures by Public Entities (Enterprises) about Transfers of Financial Assets and Interests in Variable Interest Entities*. This FSP amends SFAS 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities a replacement of FASB Statement 125,* to require public entities to provide additional disclosures that primarily focus on the transferor s continuing involvement with transferred financial assets and the related risks retained. This FSP also amends FIN 46(R), *Consolidation of Variable Interest Entities an interpretation of ARB No. 51,* to require public entities, including sponsors that have a variable interest in a variable interest entity, to provide additional disclosures about involvement with variable interest entities. Further, a nontransferor public enterprise is required to provide certain disclosures if it is either (1) the sponsor of a qualifying special-purpose entity (QSPE) and holds a variable interest in the QSPE or (2) the servicer of a QSPE and holds a significant variable interest. FSP FAS 140-4 and FIN 46(R)-8 is effective for annual and interim periods ending after December 15, 2008. The disclosures required by this FSP are included in the Notes to Consolidated Financial Statements.

Standards not yet adopted as of December 31, 2008

In December 2007, the FASB issued SFAS 141(R), *Business Combinations,* which is a revision of SFAS 141, *Business Combinations*. SFAS 141(R) establishes principles and requirements for how an acquirer in a business combination: recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree; recognizes and measures the goodwill acquired in the business combination or a gain from a bargain purchase; and discloses information to enable users of the financial statements to evaluate the nature and financial effects of the business combination. This Statement is effective for fiscal years beginning after December 15, 2008, and is to be applied prospectively. SFAS 141(R) will not have a material impact on prior acquisitions, but could have a material impact to the consolidated financial statements for business combinations entered into after the effective date.

In December 2007, the FASB issued SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements*. SFAS 160 amends Accounting Research Bulletin 51, *Consolidated Financial Statements,* to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This Statement clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be clearly reported as equity in the consolidated financial statements. Additionally, SFAS 160 requires that the amount of consolidated net income attributable to the parent and to the noncontrolling interest be clearly identified and presented on the face of the consolidated statement of income. The provisions of this Statement are effective on a prospective basis for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008, except for the presentation and disclosure requirements, which are required to be applied retrospectively. Early adoption is not permitted. Upon adoption of SFAS 160, the Company will no longer report the noncontrolling interest (previously referred to as minority interest) attributable to the REIT preferred securities between liabilities and equity on the Consolidated Statements of Condition. Rather, the noncontrolling interest attributable to the REIT preferred securities will be reported within equity, separately from the Company s equity. Additionally, the dividends paid to the REIT preferred shareholders, historically reported in the Consolidated Statements of Income as minority interest expense, will be reported as noncontrolling interest in the Consolidated Statements of Changes in Stockholders Equity, separately from changes in the Company s common equity. On the Consolidated Statements of Income, the amount of consolidated net income attributable to the parent and to the noncontrolling interest will be clearly identified and presented. These changes in presentation are effective for Colonial on January 1, 2009 and will be reflected in the Company s first quarter 2009 results. As required by SFAS 160, these changes in presentation will be retrospectively applied for all periods presented.

In March 2008, the FASB issued SFAS 161, *Disclosures about Derivative Instruments and Hedging Activities*. SFAS 161 amends SFAS 133, *Accounting for Derivative Instruments and Hedging Activities,* by requiring expanded disclosures about an entity s derivative instruments and hedging activities, but does not change SFAS 133 s scope or accounting. This Statement requires enhanced disclosures about how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for under SFAS 133 and its related interpretations, and how derivative instruments and related hedged items affect an entity s financial position, financial performance and cash flows. To meet those objectives, this Statement requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures in a tabular format about fair value amounts of and gains and losses on derivative instruments including specific disclosures regarding the location and amounts of derivative instruments in the financial statements, and disclosures about credit risk related contingent features in derivative agreements. SFAS 161 also amends SFAS 107, *Disclosures about Fair Value of Financial Instruments*, to clarify that derivative instruments are subject to the SFAS 107 concentration of credit risk disclosures. The provisions of this Statement are effective for fiscal years and interim periods beginning after November 15, 2008, and earlier application is permitted. Because SFAS 161 only requires additional disclosures, the adoption of the standard will not impact the Company s financial condition, results of operations or cash flows.

In June 2008, the FASB issued FSP EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities*. FSP EITF 03-6-1 addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and therefore need to be included in the earnings allocation in calculating earnings per share under the two-class method described in SFAS 128, *Earnings per Share*. This FSP requires companies to treat unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) as a separate class of securities in calculating earnings per share. The provisions of this FSP are effective for fiscal years beginning after December 15, 2008; earlier application is not permitted. Upon adoption of this FSP during the first quarter of 2009, all prior-period earnings per share data presented must be adjusted retrospectively to conform to the provisions of this FSP. The impact of FSP EITF 03-6-1 on earnings per share is expected to be immaterial.

In June 2008, the EITF reached a final consensus on Issue 08-3, *Accounting by Lessees for Maintenance Deposits*. EITF 08-3 stipulates that a maintenance deposit should be accounted for as a deposit asset when paid to the lessor if it is probable that the deposit will be refunded to the lessee. If it is determined that a maintenance deposit is less than probable of being refunded to the lessee, the deposit should be recognized as additional expense. If it is probable at inception of the lease that a portion of the deposit will not be refunded, the lessee should recognize as expense a pro-rata portion of the deposit as it is paid. The cost of maintenance activities should be expensed or capitalized by the lessee, as appropriate, when the underlying maintenance is performed. This consensus is effective for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Early application is not permitted. The effect of applying this consensus must be recognized as a cumulative effect of a change in accounting principle as of the beginning of the fiscal year in which the consensus is initially applied for all arrangements existing at the effective date. The impact of applying EITF 08-3 is expected to be immaterial.

In November 2008, the EITF reached a final consensus on Issue 08-6, *Equity Method Investment Accounting Considerations*. EITF 08-6 stipulates that an entity should determine the initial carrying value of an equity method investment by applying the cost accumulation model described in SFAS 141(R) and should use the other-than-temporary impairment model described in Accounting Principles Board (APB) Opinion 18, *The Equity Method of Accounting for Investments in Common Stock*, when testing equity method investments for impairment. However, investors should adjust any impairments recorded by an investee for existing differences between the investor s basis and the underlying investee s basis in such impaired assets. Share issuances by the investee should be accounted for as if the equity method investor had sold a proportionate share of its investment (i.e., any gain or loss is recognized in earnings). When an investment is no longer within the scope of equity method accounting and instead is within the scope of cost method accounting or SFAS 115, *Accounting for Certain Investments in Debt and Equity Securities*, the investor should prospectively apply the provisions of APB

Opinion 18 or SFAS 115 and use the current carrying amount of the investment as its initial cost. EITF 08-6 is effective for fiscal years beginning on or after December 15, 2008, and interim periods within those fiscal years, which is consistent with the effective dates of SFAS 141(R) and SFAS 160. This EITF should be applied prospectively and earlier application by an entity that has previously adopted an alternative accounting policy is not permitted. The impact of applying EITF Issue 08-6 is expected to be immaterial.

In December 2008, the FASB issued FSP FAS 132(R)-1*, Employers Disclosures about Postretirement Benefit Plan Assets*. This FSP contains amendments to SFAS 132(R), *Employers Disclosures about Pensions and Other Postretirement Benefits*, which are intended to enhance the transparency surrounding the types of assets and associated risks in an employer s defined benefit pension or other postretirement plan. This FSP expands the SFAS 132(R) disclosures by adding required disclosures about: (1) how investment allocation decisions are made by management, (2) major categories of plan assets, and (3) significant concentrations of risk. Additionally, this FSP requires an employer to disclose information about the valuation of plan assets similar to that required under SFAS 157. Those disclosures include: (1) the level within the fair value hierarchy in which fair value measurements of plan assets fall, (2) information about the inputs and valuation techniques used to measure the fair value of plan assets, and (3) a reconciliation of the beginning and ending balances of plan assets valued using significant unobservable inputs (Level 3 under SFAS 157). The new disclosures are required to be included in financial statements for fiscal years ending after December 15, 2009. Because FSP FAS 132(R)-1 only requires additional disclosures, the adoption of the standard will not impact the Company s financial condition, results of operations or cash flows.

COMPARISON OF 2007 WITH 2006

Colonial reported earnings for the year ended December 31, 2007 of $1.17 per diluted share, a 32% decrease from 2006. The Company also reported net income of $181 million for the year ended 2007, a 32% decrease from 2006.

The Company s net interest income, on a tax equivalent basis, increased $11.1 million, or 1%, in 2007 compared to 2006. The increase in net interest income was primarily caused by increased volumes of average earning assets coupled with a modest increase in yields. Average earning assets grew $1.2 billion, or 6%, while the yield on average earning assets increased 8 basis points to 7.22%. Net interest margin decreased to 3.55% in 2007 compared to 3.71% in 2006.

Noninterest income for 2007 decreased 2% from 2006 due to $36.0 million of securities restructuring charges incurred in 2007. However, core noninterest income increased by $27.8 million, or 15%, from 2006 to 2007, with strong increases in retail banking fees, wealth management services, mortgage banking origination and sales and bank-owned life insurance.

Noninterest expenses increased 8% in 2007 compared to 2006.

Nonperforming assets increased to $121.9 million at December 31, 2007. Colonial s nonperforming assets ratio ended 2007 at 0.86%. Net charge-offs as a percent of average net loans were 0.35% for 2007. Colonial increased its allowance for loan losses to $238.8 million at December 31, 2007 compared to $174.9 million at December 31, 2006. The allowance for loan losses as a percentage of net loans at December 31, 2007, was 1.50% compared to 1.13% at December 31, 2006.

BancGroup s total risk-based capital ratio at December 31, 2007 was 11.01% and its Tier I risk-based capital ratio was 8.22%. The Company s total and Tier I risk-based capital ratios at December 31, 2006 were 11.77% and 9.09%, respectively. The Company s Tier I leverage ratios were 6.67% and 7.81% at December 31, 2007 and 2006, respectively.

In 2007, the Company paid dividends of $115.0 million, or $0.75 per share, compared to $104.8 million, or $0.68 per share, in 2006.

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Item 7A. ***Quantitative and Qualitative Disclosures about Market Risk***

This information is included in *Management s Discussion and Analysis of Financial Condition and Results of Operations*.

Item 8. ***Financial Statements and Supplementary Data***

The financial statements and supplementary data required by Regulation S-X and by Item 302 of Regulation S-K are set forth in the pages listed below.

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Report of Independent Registered Public Accounting Firm

To Board of Directors and Shareholders

The Colonial BancGroup, Inc.:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of The Colonial BancGroup, Inc. and its subsidiaries at December 31, 2008 and 2007 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2008 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for these financial statements and for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management s Report on Internal Control over Financial Reporting. Our responsibility is to express opinions on these financial statements and on the Company s internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included 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, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

Birmingham, Alabama

March 2, 2009

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THE COLONIAL BANCGROUP, INC.

CONSOLIDATED STATEMENTS OF CONDITION

	December 31, 2008	December 31, 2007
	(In thousands)	
ASSETS		
Cash and due from banks	**$ 482,755**	$ 474,948
Interest bearing deposits in banks and the Federal Reserve	**1,534,463**	28,993
Federal funds sold	**7,642**	71,167
Securities purchased under agreements to resell	**1,556,157**	2,049,664
Securities available for sale	**3,302,959**	3,681,282
Held to maturity securities (fair value: 2008, $206,593; 2007, $1,361)	**200,421**	1,228
Loans held for sale (includes $1,950,445 measured at fair value at December 31, 2008)	**2,082,248**	1,544,222
Total loans, net of unearned income	**14,530,018**	15,923,178
Less: Allowance for loan losses	**(325,000)**	(238,845)
Loans, net	**14,205,018**	15,684,333
Premises and equipment, net	**565,769**	500,558
Goodwill	**432,053**	1,008,168
Other intangible assets, net	**49,609**	63,437
Other real estate owned	**127,850**	15,760
Bank-owned life insurance	**494,983**	475,593
Accrued interest and other assets	**774,379**	376,636
Total	**$ 25,816,306**	$ 25,975,989
LIABILITIES AND SHAREHOLDERS EQUITY		
Noninterest bearing transaction accounts	**$ 2,816,699**	$ 2,988,457
Interest bearing transaction accounts	**5,173,208**	6,783,116
Total transaction accounts	**7,989,907**	9,771,573
Time deposits	**9,117,388**	7,248,153
Brokered time deposits	**1,297,651**	1,455,586
Reciprocal brokered time deposits	**268,319**	68,955
Total brokered time deposits	**1,565,970**	1,524,541
Total deposits	**18,673,265**	18,544,267
Repurchase agreements	**472,706**	568,721
Other short-term borrowings	**700,000**	
Subordinated debt	**615,336**	386,434
Junior subordinated debt	**108,248**	108,256
Other long-term debt	**3,320,223**	3,529,146
Accrued expenses and other liabilities	**288,492**	272,536
Total liabilities	**24,178,270**	23,409,360
Minority interest/REIT preferred securities	**293,058**	293,058
Contingencies and commitments (Note 10)		
Preferred stock, $2.50 par value; 50,000,000 shares authorized and none issued at both December 31, 2008 and December 31, 2007		
Preference stock, $2.50 par value; 1,000,000 shares authorized and none issued at both December 31, 2008 and December 31, 2007		
	531,022	418,518

Common stock, $2.50 par value; 400,000,000 shares authorized; 212,408,915 and 167,407,169 shares issued and 202,442,188 and 157,440,442 shares outstanding at December 31, 2008 and December 31, 2007, respectively		
Additional paid in capital	**1,231,343**	1,004,888
Retained earnings	**145,339**	1,094,916
Treasury stock, at cost (9,966,727 shares at December 31, 2008 and December 31, 2007)	**(240,336)**	(240,336)
Accumulated other comprehensive loss, net of taxes	**(322,390)**	(4,415)
Total shareholders equity	**1,344,978**	2,273,571
Total	**$ 25,816,306**	$ 25,975,989

See Notes to Consolidated Financial Statements

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THE COLONIAL BANCGROUP, INC.

CONSOLIDATED STATEMENTS OF INCOME

	Year ended December 31, 2008	2007	2006
	(In thousands, except per share amounts)		
Interest Income:			
Interest and fees on loans	**$ 1,063,395**	$ 1,278,259	$ 1,258,513
Interest and dividends on securities:			
Taxable	**189,199**	150,950	141,918
Nontaxable	**15,001**	11,099	2,046
Dividends	**8,337**	11,963	8,498
Interest on federal funds sold and other short-term investments	**109,895**	104,214	44,610
Total interest income	**1,385,827**	1,556,485	1,455,585
Interest Expense:			
Interest on deposits	**497,023**	554,833	469,289
Interest on short-term borrowings	**27,515**	67,913	94,791
Interest on long-term debt	**197,776**	172,365	136,238
Total interest expense	**722,314**	795,111	700,318
Net Interest Income	**663,513**	761,374	755,267
Provision for loan losses	**728,942**	106,450	22,142
Net Interest Income After Provision for Loan Losses	**(65,429)**	654,924	733,125
Noninterest Income:			
Service charges on deposit accounts	**76,058**	75,466	65,071
Electronic banking	**20,363**	18,815	17,212
Other retail banking fees	**9,417**	12,275	14,436
Retail banking fees	**105,838**	106,556	96,719
Mortgage banking origination and sales	**29,951**	14,923	13,540
Wealth management services	**17,930**	16,734	14,054
Mortgage warehouse fees	**5,235**	22,240	25,323
Bank-owned life insurance	**19,395**	20,230	15,954
Securities and derivatives gains (losses), net	**3,043**	4,047	4,772
Securities restructuring charges		(36,006)	
Gain on sale of mortgages and businesses		8,750	2,829
Other income	**22,504**	28,750	16,031
Total noninterest income	**203,896**	186,224	189,222
Noninterest Expense:			