ASSURED GUARANTY LTD
Form 10-Q
August 04, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

ý QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended June 30, 2016
Or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition Period from to
Commission File No. 001-32141
ASSURED GUARANTY LTD.
(Exact name of registrant as specified in its charter)

Bermuda	98-0429991
(State or other jurisdiction of incorporation)	(I.R.S. employer identification no.)

30 Woodbourne Avenue
Hamilton HM 08
Bermuda
(Address of principal executive offices)
(441) 279-5700
(Registrant's telephone number, including area code)

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 o

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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

The number of registrant's Common Shares ($0.01 par value) outstanding as of August 2, 2016 was 132,122,615 (includes 58,858 unvested restricted shares).

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
Assured Guaranty Ltd.

Consolidated Balance Sheets (unaudited)

(dollars in millions except per share and share amounts)

	As of June 30, 2016	As of December 31, 2015
Assets		
Investment portfolio:		
Fixed-maturity securities, available-for-sale, at fair value (amortized cost of $9,401 and $10,275)	$9,960	$ 10,627
Short-term investments, at fair value	585	396
Other invested assets	170	169
Total investment portfolio	10,715	11,192
Cash	190	166
Premiums receivable, net of commissions payable	623	693
Ceded unearned premium reserve	228	232
Deferred acquisition costs	110	114
Reinsurance recoverable on unpaid losses	82	69
Salvage and subrogation recoverable	323	126
Credit derivative assets	36	81
Deferred tax asset, net	235	276
Current income tax receivable	—	40
Financial guaranty variable interest entities' assets, at fair value	814	1,261
Funds restricted for CIFG acquisition	451	—
Other assets	285	294
Total assets	$14,092	$ 14,544
Liabilities and shareholders' equity		
Unearned premium reserve	$3,617	$ 3,996
Loss and loss adjustment expense reserve	1,268	1,067
Reinsurance balances payable, net	56	51
Long-term debt	1,303	1,300
Credit derivative liabilities	432	446
Current income tax payable	19	—
Financial guaranty variable interest entities' liabilities with recourse, at fair value	790	1,225
Financial guaranty variable interest entities' liabilities without recourse, at fair value	115	124
Other liabilities	242	272
Total liabilities	7,842	8,481
Commitments and contingencies (See Note 14)		
Common stock ($0.01 par value, 500,000,000 shares authorized; 132,814,422 and 137,928,552 shares issued and outstanding)	1	1
Additional paid-in capital	1,213	1,342
Retained earnings	4,648	4,478
Accumulated other comprehensive income, net of tax of $147 and $104	383	237
Deferred equity compensation (320,193 and 320,193 shares)	5	5

Total shareholders' equity	6,250	6,063
Total liabilities and shareholders' equity	$14,092	$ 14,544

The accompanying notes are an integral part of these consolidated financial statements.

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Assured Guaranty Ltd.

Consolidated Statements of Operations (unaudited)

(dollars in millions except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenues				
Net earned premiums	$214	$219	$397	$361
Net investment income	98	98	197	199
Net realized investment gains (losses):				
Other-than-temporary impairment losses	(8)	(11)	(28)	(16)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	(3)	1	(7)	3
Net impairment loss	(5)	(12)	(21)	(19)
Other net realized investment gains (losses)	15	3	18	26
Net realized investment gains (losses)	10	(9)	(3)	7
Net change in fair value of credit derivatives:				
Realized gains (losses) and other settlements	24	8	32	29
Net unrealized gains (losses)	39	82	(29)	185
Net change in fair value of credit derivatives	63	90	3	214
Fair value gains (losses) on committed capital securities	(11)	23	(27)	25
Fair value gains (losses) on financial guaranty variable interest entities	4	5	22	(2)
Bargain purchase gain and settlement of pre-existing relationships	—	214	—	214
Other income (loss)	18	55	52	46
Total revenues	396	695	641	1,064
Expenses				
Loss and loss adjustment expenses	102	188	192	206
Amortization of deferred acquisition costs	5	6	9	10
Interest expense	25	26	51	51
Other operating expenses	63	66	123	122
Total expenses	195	286	375	389
Income (loss) before income taxes	201	409	266	675
Provision (benefit) for income taxes				
Current	32	24	62	37
Deferred	23	88	(1)	140
Total provision (benefit) for income taxes	55	112	61	177
Net income (loss)	$146	$297	$205	$498
Earnings per share:				
Basic	$1.09	$1.97	$1.52	$3.25
Diluted	$1.09	$1.96	$1.51	$3.23
Dividends per share	$0.13	$0.12	$0.26	$0.24

The accompanying notes are an integral part of these consolidated financial statements.

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Assured Guaranty Ltd.

Consolidated Statements of Comprehensive Income (unaudited)

(in millions)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income (loss)	$146	$297	$205	$498
Unrealized holding gains (losses) arising during the period on:				
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $31, $(54), $62 and $(53)	84	(136)	179	(118)
Investments with other-than-temporary impairment, net of tax provision (benefit) of $(3), $(1), $(13) and $(3)	(6)	(6)	(23)	(8)
Unrealized holding gains (losses) arising during the period, net of tax	78	(142)	156	(126)
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $4, $(4), $0 and $2	5	(5)	(1)	5
Change in net unrealized gains on investments	73	(137)	157	(131)
Other, net of tax provision	(9)	6	(11)	0
Other comprehensive income (loss)	$64	$(131)	$146	$(131)
Comprehensive income (loss)	$210	$166	$351	$367

The accompanying notes are an integral part of these consolidated financial statements.

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Assured Guaranty Ltd.

Consolidated Statement of Shareholders' Equity (unaudited)

For the Six Months Ended June 30, 2016

(dollars in millions, except share data)

	Common Shares Outstanding	Common Stock Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Deferred Equity Compensation	Total Shareholders' Equity
Balance at December 31, 2015	137,928,552	$ 1	$ 1,342	$ 4,478	$ 237	$ 5	$ 6,063
Net income	—	—	—	205	—	—	205
Dividends ($0.26 per share)	—	—	—	(35)	—	—	(35)
Common stock repurchases	(5,370,402)	0	(135)	—	—	—	(135)
Share-based compensation and other	256,272	0	6	—	—	—	6
Other comprehensive income	—	—	—	—	146	—	146
Balance at June 30, 2016	132,814,422	$ 1	$ 1,213	$ 4,648	$ 383	$ 5	$ 6,250

The accompanying notes are an integral part of these consolidated financial statements.

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Assured Guaranty Ltd.

Consolidated Statements of Cash Flows (unaudited)

(in millions)

	Six Months Ended June 30,	
	2016	2015
Net cash flows provided by (used in) operating activities	$(47)	$105
Investing activities		
Fixed-maturity securities:		
Purchases	(510)	(1,172)
Sales	739	1,381
Maturities	645	411
Net sales (purchases) of short-term investments	(190)	382
Net proceeds from paydowns on financial guaranty variable interest entities' assets	556	70
Acquisition of Radian Asset, net of cash acquired	—	(800)
Cash restricted for CIFG acquisition (see Note 2)	(451)	—
Other	(12)	27
Net cash flows provided by (used in) investing activities	777	299
Financing activities		
Dividends paid	(35)	(37)
Repurchases of common stock	(135)	(285)
Share activity under option and incentive plans	(1)	(2)
Net paydowns of financial guaranty variable interest entities' liabilities	(531)	(78)
Repayment of long-term debt	(1)	(2)
Net cash flows provided by (used in) financing activities	(703)	(404)
Effect of foreign exchange rate changes	(3)	0
Increase (decrease) in cash	24	0
Cash at beginning of period	166	75
Cash at end of period	$190	$75
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$1	$51
Interest	$48	$48

The accompanying notes are an integral part of these consolidated financial statements.

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Assured Guaranty Ltd.

Notes to Consolidated Financial Statements (unaudited)

June 30, 2016

1. Business and Basis of Presentation

Business

Assured Guaranty Ltd. (“AGL” and, together with its subsidiaries, “Assured Guaranty” or the “Company”) is a Bermuda-based holding company that provides, through its operating subsidiaries, credit protection products to the United States (“U.S.”) and international public finance (including infrastructure) and structured finance markets. The Company applies its credit underwriting judgment, risk management skills and capital markets experience to offer financial guaranty insurance that protects holders of debt instruments and other monetary obligations from defaults in scheduled payments. If an obligor defaults on a scheduled payment due on an obligation, including a scheduled principal or interest payment (“debt service”), the Company is required under its unconditional and irrevocable financial guaranty to pay the amount of the shortfall to the holder of the obligation. The Company markets its financial guaranty insurance directly to issuers and underwriters of public finance and structured finance securities as well as to investors in such obligations. The Company guarantees obligations issued principally in the U.S. and the United Kingdom ("U.K."), and also guarantees obligations issued in other countries and regions, including Australia and Western Europe.

In the past, the Company sold credit protection by issuing policies that guaranteed payment obligations under credit derivatives, primarily credit default swaps ("CDS"). Financial guaranty contracts accounted for as credit derivatives are generally structured such that the circumstances giving rise to the Company’s obligation to make loss payments are similar to those for financial guaranty insurance contracts. The Company’s credit derivative transactions are governed by International Swaps and Derivative Association, Inc. (“ISDA”) documentation. The Company has not entered into any new CDS in order to sell credit protection since the beginning of 2009, when regulatory guidelines were issued that limited the terms under which such protection could be sold. The capital and margin requirements applicable under the Dodd-Frank Wall Street Reform and Consumer Protection Act also contributed to the Company not entering into such new CDS since 2009. The Company actively pursues opportunities to terminate existing CDS, which have the effect of reducing future fair value volatility in income and/or reducing rating agency capital charges.

Basis of Presentation

The unaudited interim consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) and, in the opinion of management, reflect all adjustments that are of a normal recurring nature, necessary for a fair statement of the financial condition, results of operations and cash flows of the Company and its consolidated variable interest entities (“VIEs”) for the periods presented. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. These unaudited interim consolidated financial statements are as of June 30, 2016 and cover the three-month period ended June 30, 2016 ("Second Quarter 2016"), the three-month period ended June 30, 2015 ("Second Quarter 2015"), the six-month period ended June 30, 2016 ("Six Months 2016") and the six-month period ended June 30, 2015 ("Six Months 2015"). Certain financial information that is normally included in annual financial statements prepared in accordance with GAAP, but is not required for interim reporting purposes, has been condensed or omitted. The year-end balance sheet data was derived from audited financial

statements.

The unaudited interim consolidated financial statements include the accounts of AGL, its direct and indirect subsidiaries (collectively, the “Subsidiaries”), and its consolidated VIEs. Intercompany accounts and transactions between and among all consolidated entities have been eliminated. Certain prior year balances have been reclassified to conform to the current year's presentation.

These unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements included in AGL’s Annual Report on Form 10-K for the year ended December 31, 2015, filed with the U.S. Securities and Exchange Commission (the “SEC”).

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The Company's principal insurance company subsidiaries are:

- Assured Guaranty Municipal Corp. ("AGM"), domiciled in New York;
- Municipal Assurance Corp. ("MAC"), domiciled in New York;
- Assured Guaranty Corp. ("AGC"), domiciled in Maryland;
- Assured Guaranty (Europe) Ltd. ("AGE"), organized in the United Kingdom; and
- Assured Guaranty Re Ltd. (“AG Re”), domiciled in Bermuda.

The Company’s organizational structure includes various holding companies, two of which - Assured Guaranty US Holdings Inc. (“AGUS”) and Assured Guaranty Municipal Holdings Inc. (“AGMH”) - have public debt outstanding. See Note 15, Long-Term Debt and Credit Facilities and Note 18, Subsidiary Information.

Future Application of Accounting Standards

Credit Losses on Financial Instruments

In June 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The amendments in this ASU are intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The ASU requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions will use forward-looking information to better inform their credit loss estimates as a result of the ASU. While many of the loss estimation techniques applied today will still be permitted, the inputs to those techniques will change to reflect the full amount of expected credit losses. The ASU requires enhanced disclosures to help investors and other financial statement users to better understand significant estimates and judgments used in estimating credit losses, as well as credit quality and underwriting standards of an organization’s portfolio.

In addition, the ASU amends the accounting for credit losses on available-for-sale securities and purchased financial assets with credit deterioration. The ASU makes targeted improvements to the existing “other than temporary” impairment model for certain available-for-sale debt securities to eliminate the concept of “other than temporary” from that model. Accordingly, the ASU states that an entity must use an allowance approach, must limit the allowance to an amount at which the security’s fair value is less than its amortized cost basis, may not consider the length of time fair value has been less than amortized cost, and may not consider recoveries in fair value after the balance sheet date when assessing whether a credit loss exists. For purchased financial assets with credit deterioration, the ASU requires an entity’s method for measuring credit losses to be consistent with its method for measuring expected losses for originated and purchased non-credit-deteriorated assets.

The ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. For most debt instruments, entities will be required to record a cumulative-effect adjustment to the statement of financial position as of the beginning of the first reporting period in which the guidance is adopted. The changes to the impairment model for available-for-sale securities and changes to purchased financial assets with credit deterioration are to be applied prospectively. For the Company, this would be as of January 1, 2020. Early adoption is permitted for fiscal years, and interim periods with those fiscal years, beginning after December 15, 2018. The Company is currently evaluating the effect on its Consolidated Financial Statements of adopting this ASU.

Share-Based Payments

In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation (Topic 718) - Improvements to Employee Share-Based Payment, which simplifies several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The new guidance will require all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. It also will allow an employer to repurchase more of an employee's shares than it can today for tax withholding purposes without triggering liability accounting and to make a policy election to account for forfeitures as they occur. The ASU is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and early adoption is permitted. The Company is currently evaluating the effect on its Consolidated Financial Statements of adopting this ASU.

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2. Acquisitions

Consistent with one of its key business strategies of supplementing its book of business through acquisitions, the Company has acquired two financial guaranty companies since January 1, 2015.

CIFG Holding Inc.

On July 1, 2016, AGC acquired all of the issued and outstanding capital stock of CIFG Holding Inc., the parent of financial guaranty insurer CIFG Assurance North America, Inc. ("CIFG") (the "CIFG Acquisition"), in accordance with the agreement announced on April 13, 2016. AGC transferred $450.6 million in cash to a paying agent on June 30, 2016, in anticipation of closing; the Company recorded this transaction as funds restricted for the CIFG Acquisition on the consolidated balance sheet as of June 30, 2016. AGC caused the acquisition to be consummated on July 1, 2016 and merged CIFG with and into AGC, with AGC as the surviving company, on July 5, 2016. The CIFG Acquisition added $4.4 billion of net par insured on July 1, 2016.

The Company is in the process of allocating the purchase price to the assets acquired and liabilities assumed and conforming accounting policies but has not yet completed the acquisition date balance sheet. The Company intends to include this information in its third quarter 2016 Form 10-Q.

Radian Asset Assurance Inc.

On April 1, 2015, AGC completed the acquisition (“Radian Asset Acquisition”) of all of the issued and outstanding capital stock of financial guaranty insurer Radian Asset Assurance Inc. (“Radian Asset”) for $804.5 million. Radian Asset was merged with and into AGC, with AGC as the surviving company of the merger. The Radian Asset Acquisition added $13.6 billion to the Company's net par outstanding on April 1, 2015.

Please refer to Note 2, Acquisition of Radian Asset Assurance Inc., in Part II, Item 8. “Financial Statements and Supplementary Data” of AGL’s Annual Report on Form 10-K for the year ended December 31, 2015 for additional information on the acquisition of Radian Asset, including the purchase price and the allocation of the purchase price to net assets acquired and the resulting bargain purchase gain and the gains on settlement of pre-existing relationships.

3. Rating Actions

When a rating agency assigns a public rating to a financial obligation guaranteed by one of AGL’s insurance company subsidiaries, it generally awards that obligation the same rating it has assigned to the financial strength of the AGL subsidiary that provides the guaranty. Investors in products insured by AGL’s insurance company subsidiaries frequently rely on ratings published by the rating agencies because such ratings influence the trading value of securities and form the basis for many institutions’ investment guidelines as well as individuals’ bond purchase decisions. Therefore, the Company manages its business with the goal of achieving strong financial strength ratings. However, the methodologies and models used by rating agencies differ, presenting conflicting goals that may make it inefficient or impractical to reach the highest rating level. The methodologies and models are not fully transparent, contain subjective elements and data (such as assumptions about future market demand for the Company’s products) and change frequently. Ratings are subject to continuous review and revision or withdrawal at any time. If the financial strength ratings of one (or more) of the Company’s insurance subsidiaries were reduced below current levels, the Company expects it could have adverse effects on the impacted subsidiary's future business opportunities as well as the premiums the impacted subsidiary could charge for its insurance policies.

The Company periodically assesses the value of each rating assigned to each of its companies, and as a result of such assessment may request that a rating agency add or drop a rating from certain of its companies. For example, the Kroll

Bond Rating Agency ("KBRA") ratings were first assigned to MAC in 2013 and to AGM in 2014 and the A.M. Best Company, Inc. ("Best") rating was first assigned to Assured Guaranty Re Overseas Ltd. ("AGRO") in 2015, while a Moody's Investors Service, Inc. ("Moody's") rating was never requested for MAC and was dropped from AG Re and AGRO in 2015.

In the last several years, Standard & Poor's Ratings Services ("S&P") and Moody's have changed, multiple times, their financial strength ratings of AGL's insurance subsidiaries, or changed the outlook on such ratings. More recently, KBRA and Best have assigned financial strength ratings to some of AGL's insurance subsidiaries. The rating agencies' most recent actions related to AGL's insurance subsidiaries are:

- On July 27, 2016, S&P affirmed the AA (stable) financial strength ratings of AGL's insurance subsidiaries.

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- On July 8, 2016 and December 10, 2015, KBRA affirmed the AA+ (stable outlook) financial strength ratings of MAC and AGM, respectively.

- On May 27, 2016, Best affirmed the A+ (stable) financial strength rating, which is their second highest rating, of AGRO.

- On December 8, 2015, Moody's published credit opinions maintaining its existing insurance financial strength ratings of A2 (stable outlook) on AGM and AGE and A3 (negative outlook) on AGC and AGC's subsidiary Assured Guaranty (UK) Ltd. ("AGUK"). Effective April 8, 2015, at the Company's request, Moody’s withdrew the financial strength ratings it had assigned to AG Re and AGRO.

There can be no assurance that any of the rating agencies will not take negative action on their financial strength ratings of AGL's insurance subsidiaries in the future.

For a discussion of the effects of rating actions on the Company, see the following:

- Note 6, Financial Guaranty Insurance
- Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives
- Note 13, Reinsurance and Other Monoline Exposures
- Note 15, Long-Term Debt and Credit Facilities

4. Outstanding Exposure

The Company’s financial guaranty contracts are written in either insurance or credit derivative form, but collectively are considered financial guaranty contracts. The Company seeks to limit its exposure to losses by underwriting obligations that it views as investment grade at inception, although, as part of its loss mitigation strategy for existing troubled credits, it may underwrite new issuances that it views as below-investment-grade ("BIG"). The Company diversifies its insured portfolio across asset classes and, in the structured finance portfolio, requires rigorous subordination or collateralization requirements. Reinsurance may be used in order to reduce net exposure to certain insured transactions.

Public finance obligations insured by the Company consist primarily of general obligation bonds supported by the taxing powers of U.S. state or municipal governmental authorities, as well as tax-supported bonds, revenue bonds and other obligations supported by covenants from state or municipal governmental authorities or other municipal obligors to impose and collect fees and charges for public services or specific infrastructure projects. The Company also includes within public finance obligations those obligations backed by the cash flow from leases or other revenues from projects serving substantial public purposes, including utilities, toll roads, health care facilities and government office buildings. The Company also includes within public finance similar obligations issued by territorial and non-U.S. sovereign and sub-sovereign issuers and governmental authorities.

Structured finance obligations insured by the Company are generally issued by special purpose entities, including VIEs, and backed by pools of assets having an ascertainable cash flow or market value or other specialized financial obligations. Some of these VIEs are consolidated as described in Note 9, Consolidated Variable Interest Entities. Unless otherwise specified, the outstanding par and debt service amounts presented in this note include outstanding exposures on VIEs whether or not they are consolidated.

Surveillance Categories

The Company segregates its insured portfolio into investment grade and BIG surveillance categories to facilitate the appropriate allocation of resources to monitoring and loss mitigation efforts and to aid in establishing the appropriate cycle for periodic review for each exposure. BIG exposures include all exposures with internal credit ratings below BBB-. The Company’s internal credit ratings are based on internal assessments of the likelihood of default and loss severity in the event of default. Internal credit ratings are expressed on a ratings scale similar to that used by the rating agencies and are generally reflective of an approach similar to that employed by the rating agencies, except that the Company's internal credit ratings focus on future performance rather than lifetime performance.

The Company monitors its investment grade credits to determine whether any need to be internally downgraded to BIG and refreshes its internal credit ratings on individual credits in quarterly, semi-annual or annual cycles based on the Company’s view of the credit’s quality, loss potential, volatility and sector. Ratings on credits in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter. The Company’s credit ratings on assumed credits

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are based on the Company's reviews of low-rated credits or credits in volatile sectors, unless such information is not available, in which case, the ceding company's credit rating of the transactions are used.

Credits identified as BIG are subjected to further review to determine the probability of a loss. See Note 5, Expected Loss to be Paid, for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. For surveillance purposes, the Company calculates present value using a constant discount rate of 4% or 5% depending on the insurance subsidiary. (Risk-free rates are used for calculating the expected loss for financial statement measurement purposes.)

More extensive monitoring and intervention is employed for all BIG surveillance categories, with internal credit ratings reviewed quarterly. The Company expects "future losses" on a transaction when the Company believes there is at least a 50% chance that, on a present value basis, it will pay more claims in the future of that transaction than it will have reimbursed. The three BIG categories are:

- BIG Category 1: Below-investment-grade transactions showing sufficient deterioration to make future losses possible, but for which none are currently expected.

- BIG Category 2: Below-investment-grade transactions for which future losses are expected but for which no claims (other than liquidity claims, which are claims that the Company expects to be reimbursed within one year) have yet been paid.

- BIG Category 3: Below-investment-grade transactions for which future losses are expected and on which claims (other than liquidity claims) have been paid.

Components of Outstanding Exposure

Unless otherwise noted, ratings disclosed herein on the Company's insured portfolio reflect its internal ratings. The Company classifies those portions of risks benefiting from reimbursement obligations collateralized by eligible assets held in trust in acceptable reimbursement structures as the higher of 'AA' or their current internal rating.

The Company purchases securities that it has insured, and for which it has expected losses to be paid, in order to mitigate the economic effect of insured losses ("loss mitigation securities"). The Company excludes amounts attributable to loss mitigation securities (unless otherwise indicated) from par and debt service outstanding, because it manages such securities as investments and not insurance exposure. The following table presents the gross and net debt service for all financial guaranty contracts.

Financial Guaranty
Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding	
	June 30, 2016	December 31, 2015	June 30, 2016	December 31, 2015
	(in millions)			
Public finance	$473,991	$ 515,494	$455,056	$ 494,426
Structured finance	34,814	43,976	33,306	41,915
Total financial guaranty	$508,805	$ 559,470	$488,362	$ 536,341

In addition to the amounts shown in the table above, the Company's net mortgage guaranty insurance debt service was approximately $104 million as of June 30, 2016 and $102 million as of December 31, 2015, related to loans originated in Ireland. The increase in the net mortgage guaranty insurance debt service is due to exchange rate fluctuations.

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Financial Guaranty Portfolio by Internal Rating
As of June 30, 2016

Rating Category	Public Finance U.S. Net Par Outstanding	%	Public Finance Non-U.S. Net Par Outstanding	%	Structured Finance U.S Net Par Outstanding	%	Structured Finance Non-U.S Net Par Outstanding	%	Total Net Par Outstanding	%
	(dollars in millions)									
AAA	$2,376	0.9 %	$695	2.5 %	$11,362	44.4 %	$1,628	40.1 %	$16,061	4.9 %
AA	59,310	21.8	1,775	6.3	6,719	26.3	149	3.7	67,953	20.6
A	142,028	52.2	6,440	22.9	2,008	7.9	457	11.2	150,933	45.7
BBB	60,132	22.1	17,840	63.4	920	3.6	1,235	30.4	80,127	24.3
BIG	8,268	3.0	1,378	4.9	4,553	17.8	591	14.6	14,790	4.5
Total net par outstanding (1)	$272,114	100.0%	$28,128	100.0%	$25,562	100.0 %	$4,060	100.0 %	$329,864	100.0%

(1) Excludes $1.4 billion of loss mitigation securities insured and held by the Company as of June 30, 2016, which are primarily BIG.

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2015

Rating Category	Public Finance U.S. Net Par Outstanding	%	Public Finance Non-U.S. Net Par Outstanding	%	Structured Finance U.S Net Par Outstanding	%	Structured Finance Non-U.S Net Par Outstanding	%	Total Net Par Outstanding	%
	(dollars in millions)									
AAA	$3,053	1.1 %	$709	2.4 %	$14,366	45.2 %	$2,709	50.6 %	$20,837	5.8 %
AA	69,274	23.7	2,017	6.8	7,934	25.0	177	3.3	79,402	22.1
A	157,440	53.9	6,765	22.9	2,486	7.8	555	10.3	167,246	46.7
BBB	54,315	18.6	18,708	63.2	1,515	4.8	1,365	25.5	75,903	21.2
BIG	7,784	2.7	1,378	4.7	5,469	17.2	552	10.3	15,183	4.2
Total net par outstanding (1)	$291,866	100.0%	$29,577	100.0%	$31,770	100.0 %	$5,358	100.0 %	$358,571	100.0%

(1) Excludes $1.5 billion of loss mitigation securities insured and held by the Company as of December 31, 2015, which are primarily BIG.

In addition to amounts shown in the tables above, the Company had outstanding commitments to provide guaranties of $117 million for public finance obligations as of June 30, 2016. The expiration dates for the public finance commitments range between July 1, 2016 and February 25, 2017, with $53 million expiring prior to the date of this filing. The commitments are contingent on the satisfaction of all conditions set forth in them and may expire unused or be canceled at the counterparty’s request. Therefore, the total commitment amount does not necessarily reflect actual future guaranteed amounts.

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Components of BIG Portfolio

Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of June 30, 2016

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
U.S. public finance (1)	$4,902	$3,191	$ 175	$ 8,268	$ 272,114
Non-U.S. public finance	863	515	—	1,378	28,128
Structured finance:					
First lien U.S. residential mortgage-backed securities ("RMBS"):					
Prime first lien	21	83	20	124	237
Alt-A first lien	120	42	459	621	1,090
Option ARM	27	6	63	96	186
Subprime	128	210	882	1,220	3,193
Second lien U.S. RMBS	22	73	1,271	1,366	1,376
Total U.S. RMBS	318	414	2,695	3,427	6,082
Triple-X life insurance transactions	—	—	216	216	2,189
Trust preferred securities (“TruPS”)	436	127	—	563	3,255
Student loans	—	68	42	110	1,645
Other structured finance	537	254	37	828	16,451
Total	$7,056	$4,569	$ 3,165	$ 14,790	$ 329,864

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Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of December 31, 2015

	BIG Net Par Outstanding				Net Par Outstanding
	BIG 1	BIG 2	BIG 3	Total BIG	
			(in millions)		
U.S. public finance	$4,765	$2,883	$ 136	$ 7,784	$ 291,866
Non-U.S. public finance	875	503	—	1,378	29,577
Structured finance:					
First lien U.S. RMBS:					
Prime first lien	225	34	25	284	445
Alt-A first lien	119	73	601	793	1,353
Option ARM	39	12	90	141	252
Subprime	146	228	930	1,304	3,457
Second lien U.S. RMBS	491	50	910	1,451	1,560
Total U.S. RMBS	1,020	397	2,556	3,973	7,067
Triple-X life insurance transactions	—	—	216	216	2,750
TruPS	679	127	—	806	4,379
Student loans	12	68	83	163	1,818
Other structured finance	672	151	40	863	21,114
Total	$8,023	$4,129	$ 3,031	$ 15,183	$ 358,571

(1) Subsequent to June 30, 2016, and as a result of its July 1, 2016 Puerto Rico claim payments, the Company downgraded from BIG 1 to BIG 3 $1,803 million net par outstanding of financial guaranty insurance across two risks.

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BIG Net Par Outstanding
and Number of Risks
As of June 30, 2016

	Net Par Outstanding			Number of Risks(2)		
Description	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
	(dollars in millions)					
BIG:						
Category 1 (3)	$6,546	$ 510	$7,056	198	10	208
Category 2	4,119	450	4,569	76	5	81
Category 3 (3)	3,039	126	3,165	131	12	143
Total BIG	$13,704	$ 1,086	$14,790	405	27	432

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BIG Net Par Outstanding
and Number of Risks
As of December 31, 2015

Description	Net Par Outstanding			Number of Risks(2)		
	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
	(dollars in millions)					
BIG:						
Category 1	$7,019	$ 1,004	$8,023	202	12	214
Category 2	3,655	474	4,129	85	8	93
Category 3	2,900	131	3,031	132	12	144
Total BIG	$13,574	$ 1,609	$15,183	419	32	451

(1) Includes net par outstanding for VIEs.

(2) A risk represents the aggregate of the financial guaranty policies that share the same revenue source for purposes of making debt service payments.

(3) Subsequent to June 30, 2016, and as a result of its July 1, 2016 Puerto Rico claim payments, the Company downgraded from BIG 1 to BIG 3 $1,803 million net par outstanding of financial guaranty insurance across two risks.

Exposure to Puerto Rico

The Company has insured exposure to general obligation bonds of the Commonwealth of Puerto Rico (“Puerto Rico” or the “Commonwealth”) and various obligations of its related authorities and public corporations aggregating $5.1 billion net par as of June 30, 2016, all of which are rated BIG.

Puerto Rico has experienced significant general fund budget deficits in recent years. In addition to high debt levels, Puerto Rico faces a challenging economic environment; the economy has declined nearly every year since 2007, while the population has shrunk every year since 2006 as residents have emigrated.

On June 28, 2015, Governor García Padilla of Puerto Rico (the "Governor") publicly stated that the Commonwealth’s public debt, considering the current level of economic activity, was unpayable and that a comprehensive debt restructuring might be necessary.

On November 30, 2015 and December 8, 2015, the Governor issued executive orders (“Clawback Orders”) directing the Puerto Rico Department of Treasury and the Puerto Rico Tourism Company to retain or transfer certain taxes pledged to secure the payment of bonds issued by the Puerto Rico Highways and Transportation Authority ("PRHTA"), Puerto Rico Infrastructure Financing Authority ("PRIFA"), and Puerto Rico Convention Center District Authority ("PRCCDA"). On January 7, 2016, the Company sued various Puerto Rico governmental officials in the United States District Court, District of Puerto Rico, asserting that this attempt to “claw back” pledged taxes is unconstitutional, and demanding declaratory and injunctive relief. The Puerto Rico credits insured by the Company subject to the Clawback Orders are shown in the table “Puerto Rico Net Par Outstanding” below.

On January 1, 2016, PRIFA defaulted on payment of a portion of the interest due on its bonds on that date, resulting in a claim on the Company for those PRIFA bonds the Company insures. There have been additional payment defaults on this and other Puerto Rico credits since then, including, on July 1, 2016, a default on the payment of the Commonwealth's general obligation bonds. The Company has now paid claims on several Puerto Rico credits as shown in the table "Puerto Rico Net Par Outstanding" below.

On April 6, 2016, the Governor signed into law the Puerto Rico Emergency Moratorium & Financial Rehabilitation Act (the "Moratorium Act"). The Moratorium Act purportedly empowers the Governor to declare, entity by entity, states of emergencies and moratoriums on debt service payments on obligations of the Commonwealth and its related authorities and public corporations, as well as instituting a stay against related litigation, among other things. The Governor has used the

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authority of the Moratorium Act to take a number of actions related to issuers of obligations the Company insures. National Public Finance Guarantee Corp. (another financial guarantor), holders of the Commonwealth general obligation bonds and certain Puerto Rico residents have filed suits to invalidate the Moratorium Act, and on July 21, 2016, the Company filed a motion and form of complaint in the U.S. District Court for the District of Puerto Rico seeking relief from the stay of litigation imposed by the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") to seek a declaration that the Moratorium Act is preempted by Federal bankruptcy law.

On June 13, 2016, the Supreme Court of the United States affirmed rulings of lower courts finding that the Puerto Rico Public Corporation Debt Enforcement and Recovery Act, which was enacted by Puerto Rico in June 2014 in order to provide a legislative framework for certain public corporations experiencing severe financial stress to restructure their debt, was preempted by the U.S. Bankruptcy Code and therefore void.

On June 30, 2016, PROMESA was signed into law by the President of the United States. PROMESA establishes a seven-member federal financial oversight board ("Oversight Board") with authority to require that balanced budgets and fiscal plans be adopted and implemented by Puerto Rico. PROMESA provides a legal framework under which the debt of the Commonwealth and its related authorities and public corporations may be voluntarily restructured, and grants the Oversight Board the sole authority to file restructuring petitions in a federal court to restructure the debt of the Commonwealth and its related authorities and public corporations if voluntary negotiations fail, provided that any such restructuring must be in accordance with an Oversight Board approved fiscal plan that respects the liens and priorities provided under Puerto Rico law. PROMESA also appears to preempt at least portions of the Moratorium Act and appears to stay debt-related litigation, possibly including the Company's litigation regarding the Clawback Orders. Members of the Oversight Board have yet to be named.

The final shape, timing and validity of responses to Puerto Rico's distress eventually enacted or implemented under the auspices of PROMESA and the Oversight Board or otherwise, and the impact of any such responses on obligations insured by the Company, is uncertain.

The Company groups its Puerto Rico exposure into three categories:

- Constitutionally Guaranteed. The Company includes in this category public debt benefiting from Article VI of the Constitution of the Commonwealth, which expressly provides that interest and principal payments on the public debt are to be paid before other disbursements are made.

- Public Corporations – Certain Revenues Potentially Subject to Clawback. The Company includes in this category the debt of public corporations for which applicable law permits the Commonwealth to claw back, subject to certain conditions and for the payment of public debt, at least a portion of the revenues supporting the bonds the Company insures. As a Constitutional condition to clawback, available Commonwealth revenues for any fiscal year must be insufficient to pay Commonwealth debt service before the payment of any appropriations for that year. The Company believes that this condition has not been satisfied to date, and accordingly that the Commonwealth has not to date been entitled to clawback revenues supporting debt insured by the Company. As noted above, the Company sued various Puerto Rico governmental officials in the United States District Court, District of Puerto Rico asserting that Puerto Rico's recent attempt to "claw back" pledged taxes is unconstitutional, and demanding declaratory and injunctive relief.

- Other Public Corporations. The Company includes in this category the debt of public corporations that are supported by revenues it does not believe are subject to clawback.

Constitutionally Guaranteed

General Obligation. As of June 30, 2016, the Company had $1,615 million insured net par outstanding of the general obligations of Puerto Rico, which are supported by the good faith, credit and taxing power of the Commonwealth. On July 1, 2016, despite the requirements of Article VI of its Constitution but pursuant to an executive order issued by the Governor under the Moratorium Act, the Commonwealth defaulted on most of the debt service payment due that day, and the Company made its first claim payments on these bonds.

Puerto Rico Public Buildings Authority ("PBA"). As of June 30, 2016, the Company had $188 million insured net par outstanding of PBA bonds, which are supported by a pledge of the rents due under leases of government facilities to departments, agencies, instrumentalities and municipalities of the Commonwealth, and that benefit from a Commonwealth guaranty supported by a pledge of the Commonwealth's good faith, credit and taxing power. On July 1, 2016, despite the requirements of Article VI of its Constitution but pursuant to an executive order issued by the Governor under the Moratorium

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Act, the PBA defaulted on most of the debt service payment due that day, and the Company made its first claim payments on these bonds.

Public Corporations - Certain Revenues Potentially Subject to Clawback

PRHTA. As of June 30, 2016, the Company had $910 million insured net par outstanding of PRHTA (Transportation revenue) bonds and $369 million insured net par of PRHTA (Highways revenue) bonds. The transportation revenue bonds are secured by a subordinate gross pledge of gasoline and gas oil and diesel oil taxes, motor vehicle license fees and certain tolls, plus a first lien on up to $120 million annually of taxes on crude oil, unfinished oil and derivative products. The highways revenue bonds are secured by a gross pledge of gasoline and gas oil and diesel oil taxes, motor vehicle license fees and certain tolls. The Clawback Orders cover Commonwealth-derived taxes that are allocated to PRHTA. The Company believes that such sources represented a substantial majority of PRHTA’s revenues in 2015. The PRHTA bonds are subject to executive orders issued pursuant to the Moratorium Act. As noted above, the Company filed a motion and form of complaint in the U.S. District Court for the District of Puerto Rico seeking relief from the PROMESA stay to seek a declaration that the Moratorium Act is preempted by Federal bankruptcy law and that certain gubernatorial executive orders diverting PRHTA pledged toll revenues (which are not subject to the Clawback Orders) are preempted by PROMESA and violate the U.S. Constitution, and also seeking damages and injunctive relief. There were sufficient funds in the PRHTA bond accounts to make the July 1, 2016, PRHTA debt service payments guaranteed by the Company, and those payments were made in full.

PRCCDA. As of June 30, 2016, the Company had $164 million insured net par outstanding of PRCCDA bonds, which are secured by certain hotel tax revenues. These revenues are sensitive to the level of economic activity in the area and are subject to the Clawback Orders, and the bonds are subject to an executive order issued pursuant to the Moratorium Act. There were sufficient funds in the PRCCDA bond accounts to make the July 1, 2016 PRCCDA bond payments guaranteed by the Company, and those payments were made in full.

PRIFA. As of June 30, 2016, the Company had $18 million insured net par outstanding of PRIFA bonds, which are secured primarily by the return to Puerto Rico of federal excise taxes paid on rum. These revenues are subject to the Clawback Orders and the bonds are subject to an executive order issued pursuant to the Moratorium Act. The Company made its first claim payment on PRIFA bonds in January 2016, and has continued to make claim payments on PRIFA bonds.

Other Public Corporations

Puerto Rico Electric Power Authority ("PREPA"). As of June 30, 2016, the Company had $744 million insured net par outstanding of PREPA obligations, which are payable from a pledge of net revenues of the electric system.

On December 24, 2015, AGM and AGC entered into a Restructuring Support Agreement (“RSA”) with PREPA, an ad hoc group of uninsured bondholders and a group of fuel-line lenders that would, subject to certain conditions, result in, among other things, modernization of the utility and a restructuring of current debt. Upon finalization of the contemplated restructuring transaction, insured PREPA revenue bonds (with no reduction to par or stated interest rate or extension of maturity) will be supported by securitization bonds issued by a special purpose corporation and secured by a transition charge assessed on ratepayers. To facilitate the securitization transaction and in exchange for a market premium, Assured Guaranty will issue surety insurance policies in an aggregate amount not expected to exceed $113 million ($14 million for AGC and $99 million for AGM) to support a portion of the reserve fund for the securitization bonds. Certain of the creditors also agreed, subject to certain conditions, to participate in a bridge financing, which was closed in two tranches on May 19, 2016 and June 22, 2016. AGM's and AGC's share of the bridge financing was approximately $15 million ($2 million for AGC and $13 million for AGM). Legislation meeting the requirements of the RSA was enacted on February 16, 2016, and a transition charge to be paid by PREPA rate

payers for debt service on the securitization bonds as contemplated by the RSA was approved by the Puerto Rico Energy Commission on June 20, 2016. The closing of the restructuring transaction and the issuance of the surety bonds are subject to certain conditions, including execution of acceptable documentation and legal opinions.

On July 1, 2016, PREPA made full payment of the $41 million of principal and interest due on PREPA revenue bonds insured by AGM and AGC. That payment was funded in part by AGM’s purchase of $26 million of PREPA bonds maturing in 2020. Upon finalization of the RSA, these new PREPA revenue bonds will be supported by securitization bonds contemplated by the RSA. In early 2016, PREPA repaid in full the $74 million in aggregate principal amount of PREPA revenue bonds purchased by AGM and AGC in July 2015 to replenish some of the operating funds PREPA used to make the July 2015 payments on the PREPA revenue bonds insured by AGM and AGC.

There can be no assurance that the conditions in the RSA will be met or that, if the conditions are met, the RSA's other provisions, including those related to the insured PREPA revenue bonds, will be implemented. In addition, the impact of

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PROMESA and the Moratorium Act or any attempt to exercise the power purportedly granted by the Moratorium Act on the implementation of the RSA is uncertain. PREPA, during the pendency of the agreements, has suspended deposits into its debt service fund.

Puerto Rico Aqueduct and Sewer Authority (“PRASA”). As of June 30, 2016, the Company had $388 million of insured net par outstanding to PRASA bonds, which are secured by the gross revenues of the water and sewer system. On September 15, 2015, PRASA entered into a settlement with the U.S.Department of Justice and the U.S. Environmental Protection Agency that requires it to spend $1.6 billion to upgrade and improve its sewer system island-wide. According to a material event notice PRASA filed on March 4, 2016, PRASA owed its contractors $140 million. The PRASA Revitalization Act, which establishes a securitization mechanism that could facilitate debt issuance, was signed into law on July 13, 2016. While certain bonds benefiting from a guarantee by the Commonwealth are subject to an executive order issued under the Moratorium Act, bonds insured by the Company are not subject to that order. There were sufficient funds in the PRASA bond accounts to make the July 1, 2016, PRASA bond payments guaranteed by the Company, and those payments were made in full.

Municipal Finance Agency ("MFA"). As of June 30, 2016, the Company had $387 million net par outstanding of bonds issued by MFA secured by a pledge of local property tax revenues. There were sufficient funds in the MFA bond accounts to make the July 1, 2016 MFA bond payments guaranteed by the Company, and those payments were made in full.

Puerto Rico Sales Tax Financing Corporation (“COFINA”). As of June 30, 2016, the Company had $270 million insured net par outstanding of junior COFINA bonds, which are secured primarily by a second lien on certain sales and use taxes. There were no debt service payments due on July 1, 2016 on Company-insured COFINA bonds, and, as of the date of this filing, all payments on Company-insured COFINA bonds had been made.

University of Puerto Rico (“U of PR”). As of June 30, 2016, the Company had $1 million insured net par outstanding of U of PR bonds, which are general obligations of the university and are secured by a subordinate lien on the proceeds, profits and other income of the University, subject to a senior pledge and lien for the benefit of outstanding university system revenue bonds. The U of PR bonds are subject to an executive order issued under the Moratorium Act. There were no debt service payments due on July 1, 2016 on Company-insured U of PR bonds, and, as of the date of this filing, all payments on Company-insured U of PR bonds had been made.

All Puerto Rico exposures are internally rated triple-C or below. The following tables show the Company’s insured exposure to general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations.

Puerto Rico
Gross Par and Gross Debt Service Outstanding

	Gross Par Outstanding		Gross Debt Service Outstanding	
	June 30, 2016	December 31, 2015	June 30, 2016	December 31, 2015
	(in millions)			
Exposure to Puerto Rico	$5,756	$ 5,755	$9,483	$ 9,632

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Puerto Rico
Net Par Outstanding

	As of June 30, 2016	As of December 31, 2015
	(in millions)	
Commonwealth Constitutionally Guaranteed		
Commonwealth of Puerto Rico - General Obligation Bonds (1)	$1,615	$ 1,615
Puerto Rico Public Buildings Authority (1)	188	188
Public Corporations - Certain Revenues Potentially Subject to Clawback		
PRHTA (Transportation revenue)	910	909
PRHTA (Highways revenue)	369	370
PRCCDA	164	164
PRIFA (1)	18	18
Other Public Corporations		
PREPA	744	744
PRASA	388	388
MFA	387	387
COFINA	270	269
U of PR	1	1
Total net exposure to Puerto Rico	$5,054	$ 5,053

(1) As of the date of this filing, the Company has paid claims on these credits.

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The following table shows the scheduled amortization of the insured general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations. The Company guarantees payments of interest and principal when those amounts are scheduled to be paid and cannot be required to pay on an accelerated basis. In the event that obligors default on their obligations, the Company would only be required to pay the shortfall between the principal and interest due in any given period and the amount paid by the obligors.

Amortization Schedule of Puerto Rico Net Par Outstanding
and Net Debt Service Outstanding
As of June 30, 2016

	Scheduled Net Par Amortization	Scheduled Net Debt Service Amortization
	(in millions)	
2016 (July 1 – September 30)	$302	$ 428
2016 (October 1 – December 31)	0	2
2017	222	463
2018	179	410
2019	204	424
2020	270	482
2021	125	323
2022	115	305
2023	150	338
2024	174	352
2025	196	366
2026-2030	943	1,633
2031-2035	1,131	1,599
2036-2040	579	780
2041-2045	296	380
2046-2047	168	181
Total	$5,054	$ 8,466

Exposure to Selected European Countries

The European countries where the Company has exposure and believes heightened uncertainties exist are: Hungary, Italy, Portugal, Spain and Turkey (collectively, the “Selected European Countries”). The Company added Turkey to its list of Selected European Countries as of June 30, 2016, as a result of the recent political turmoil in the country. The Company’s direct economic exposure to the Selected European Countries (based on par for financial guaranty contracts and notional amount for financial guaranty contracts accounted for as derivatives) is shown in the following table, net of ceded reinsurance.

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Net Direct Economic Exposure to Selected European Countries(1)
As of June 30, 2016

	Hungary	Italy	Portugal	Spain	Turkey	Total
	(in millions)					
Sub-sovereign exposure(2)	$265	$793	$ 80	$366	$ —	$1,504
Non-sovereign exposure(3)	174	432	—	—	204	810
Total	$439	$1,225	$ 80	$366	$ 204	$2,314
Total BIG (See Note 5)	$369	$—	$ 80	$366	$ —	$815

(1) While the Company's exposures are shown in U.S. dollars, the obligations the Company insures are in various currencies, primarily Euros.

(2) Sub-sovereign exposure in Selected European Countries includes transactions backed by receivables from or supported by sub-sovereigns, which are governmental or government-backed entities other than the ultimate governing body of the country.

(3) Non-sovereign exposure in Selected European Countries includes debt of regulated utilities, RMBS and diversified payment rights ("DPR") securitizations.

The Company has excluded from the exposure tables above its indirect economic exposure to the Selected European Countries through policies it provides on pooled corporate and commercial receivables transactions. The Company calculates indirect exposure to a country by multiplying the par amount of a transaction insured by the Company times the percent of the relevant collateral pool reported as having a nexus to the country. On that basis, the Company has calculated exposure of $203 million to Selected European Countries (plus Greece) in transactions with $3.5 billion of net par outstanding. The indirect exposure to credits with a nexus to Greece is $4 million across several highly rated pooled corporate obligations with net par outstanding of $192 million.

The $204 million net insured par exposure in Turkey is to DPR securitizations sponsored by a major Turkish bank. These DPR securitizations were established outside of Turkey and involve payment orders in U.S. dollars, pounds sterling and Euros from persons outside of Turkey to beneficiaries in Turkey who are customers of the sponsoring bank. The sponsoring bank's correspondent banks have agreed to remit all such payments to a trustee-controlled account outside Turkey, where debt service payments for the DPR securitization are given priority over payments to the sponsoring bank.

5. Expected Loss to be Paid

Loss Estimation Process

This note provides information regarding expected claim payments to be made under all contracts in the insured portfolio, regardless of the accounting model. The Company's loss reserve committees estimate expected loss to be paid for all contracts by reviewing analyses that consider various scenarios with corresponding probabilities assigned to them. Depending upon the nature of the risk, the Company's view of the potential size of any loss and the information available to the Company, that analysis may be based upon individually developed cash flow models, internal credit rating assessments and sector-driven loss severity assumptions or judgmental assessments.

The financial guaranties issued by the Company insure the credit performance of the guaranteed obligations over an extended period of time, in some cases over 30 years, and in most circumstances, the Company has no right to cancel such financial guaranties. The determination of expected loss to be paid is an inherently subjective process involving

numerous estimates, assumptions and judgments by management, using both internal and external data sources with regard to frequency, severity of loss, economic projections, governmental actions, negotiations and other factors that affect credit performance. These estimates, assumptions and judgments, and the factors on which they are based, may change materially over a quarter, and as a result the Company’s loss estimates may change materially over that same period.

The Company does not use traditional actuarial approaches to determine its estimates of expected losses. Actual losses will ultimately depend on future events or transaction performance and may be influenced by many interrelated factors that are difficult to predict. As a result, the Company's current projections of probable and estimable losses may be subject to

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considerable volatility and may not reflect the Company's ultimate claims paid. For information on the Company's loss estimation process, please refer to Note 5, Expected Losses to be Paid, of Part II, Item 8, Financial Statements and Supplementary Data in AGL's Annual Report on Form 10-K for the year ended December 31, 2015.

The following tables present a roll forward of the present value of net expected loss to be paid for all contracts, whether accounted for as insurance, credit derivatives or financial guaranty ("FG") VIEs, by sector, after the benefit for expected recoveries for breaches of representations and warranties ("R&W") and other expected recoveries. The Company used weighted average risk-free rates for U.S. dollar denominated obligations that ranged from 0.0% to 2.46% as of June 30, 2016 and 0.0% to 3.25% as of December 31, 2015.

Net Expected Loss to be Paid
After Net Expected Recoveries for Breaches of R&W
Roll Forward

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Net expected loss to be paid, beginning of period	$1,337	$1,154	$1,391	$1,169
Net expected loss to be paid on Radian Asset portfolio as of April 1, 2015	—	190	—	190
Economic loss development due to:				
Accretion of discount	6	7	15	14
Changes in discount rates	45	(47)	108	(40)
Changes in timing and assumptions	(29)	232	(42)	215
Total economic loss development	22	192	81	189
Paid losses	(33)	(26)	(146)	(38)
Net expected loss to be paid, end of period	$1,326	$1,510	$1,326	$1,510

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Net Expected Loss to be Paid
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Second Quarter 2016

	Net Expected Loss to be Paid (Recovered) as of March 31, 2016	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of June 30, 2016 (2)
	(in millions)			
Public Finance:				
U.S. public finance	$864	$ 111	$ (12)	$ 963
Non-U.S. public finance	39	(2)	—	37
Public Finance	903	109	(12)	1,000
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	(1)	0	4	3
Alt-A first lien	36	(38)	(94)	(96)
Option ARM	(47)	(10)	1	(56)
Subprime	240	(26)	13	227
Total first lien	228	(74)	(76)	78
Second lien	65	(7)	56	114
Total U.S. RMBS	293	(81)	(20)	192
Triple-X life insurance transactions	102	(2)	0	100
Student loans	32	(1)	0	31
Other structured finance	7	(3)	(1)	3
Structured Finance	434	(87)	(21)	326
Total	$1,337	$ 22	$ (33)	$ 1,326

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Net Expected Loss to be Paid
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Second Quarter 2015

	Net Expected Loss to be Paid (Recovered) as of March 31, 2015	Net Expected Loss to be Paid (Recovered) on Radian Asset portfolio as of April 1, 2015	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of June 30, 2015
	(in millions)				
Public Finance:					
U.S. public finance	$310	$ 81	$ 226	$ (4)	$ 613
Non-U.S public finance	42	4	(2)	—	44
Public Finance	352	85	224	(4)	657
Structured Finance:					
U.S. RMBS:					
First lien:					
Prime first lien	3	—	(1)	(1)	1
Alt-A first lien	289	7	(16)	(15)	265
Option ARM	(16)	0	(3)	1	(18)
Subprime	293	(4)	(6)	(10)	273
Total first lien	569	3	(26)	(25)	521
Second lien	1	1	(6)	7	3
Total U.S. RMBS	570	4	(32)	(18)	524
Triple-X life insurance transactions	165	—	2	(2)	165
Student loans	62	—	1	(5)	58
Other structured finance	5	101	(3)	3	106
Structured Finance	802	105	(32)	(22)	853
Total	$1,154	$ 190	$ 192	$ (26)	$ 1,510

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Net Expected Loss to be Paid
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Six Months 2016

	Net Expected Loss to be Paid (Recovered) as of December 31, 2015 (2)	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of June 30, 2016 (2)
	(in millions)			
Public Finance:				
U.S. public finance	$771	$ 209	$ (17)	$ 963
Non-U.S. public finance	38	(1)	—	37
Public Finance	809	208	(17)	1,000
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	(2)	0	5	3
Alt-A first lien	127	(54)	(169)	(96)
Option ARM	(28)	(31)	3	(56)
Subprime	251	(25)	1	227
Total first lien	348	(110)	(160)	78
Second lien	61	(2)	55	114
Total U.S. RMBS	409	(112)	(105)	192
Triple-X life insurance transactions	99	2	(1)	100
Student loans	54	(15)	(8)	31
Other structured finance	20	(2)	(15)	3
Structured Finance	582	(127)	(129)	326
Total	$1,391	$ 81	$ (146)	$ 1,326

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Net Expected Loss to be Paid
After Net Expected Recoveries for Breaches of R&W
Roll Forward by Sector
Six Months 2015

	Net Expected Loss to be Paid (Recovered) as of December 31, 2014	Net Expected Loss to be Paid (Recovered) on Radian Asset portfolio as of April 1, 2015	Economic Loss Development	(Paid) Recovered Losses (1)	Net Expected Loss to be Paid (Recovered) as of June 30, 2015
	(in millions)				
Public Finance:					
U.S. public finance	$303	$ 81	$ 235	$ (6)	$ 613
Non-U.S. public finance	45	4	(5)	—	44
Public Finance	348	85	230	(6)	657
Structured Finance:					
U.S. RMBS:					
First lien:					
Prime first lien	4	—	(1)	(2)	1
Alt-A first lien	304	7	(21)	(25)	265
Option ARM	(16)	0	1	(3)	(18)
Subprime	303	(4)	(7)	(19)	273
Total first lien	595	3	(28)	(49)	521
Second lien	(11)	1	0	13	3
Total U.S. RMBS	584	4	(28)	(36)	524
Triple-X life insurance transactions	161	—	7	(3)	165
Student loans	68	—	(5)	(5)	58
Other structured finance	8	101	(15)	12	106
Structured Finance	821	105	(41)	(32)	853
Total	$1,169	$ 190	$ 189	$ (38)	$ 1,510

(1) Net of ceded paid losses, whether or not such amounts have been settled with reinsurers. Ceded paid losses are typically settled 45 days after the end of the reporting period. Such amounts are recorded in reinsurance recoverable on paid losses included in other assets. The Company paid $7 million and $5 million in loss adjustment expenses ("LAE") for Second Quarter 2016 and 2015, respectively, and $9 million and $9 million in LAE for Six Months 2016 and 2015, respectively.

(2) Includes expected LAE to be paid of $8 million as of June 30, 2016 and $12 million as of December 31, 2015.

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Future Net R&W Recoverable (Payable)(1)

	As of June 30, 2016	As of December 31, 2015
	(in millions)	
U.S. RMBS:		
First lien	$ (90)	$ 0
Second lien	32	79
Total	$ (58)	$ 79

(1) The Company's agreements with R&W providers generally provide that, as the Company makes claim payments, the R&W providers reimburse it for those claims; if the Company later receives reimbursement through the transaction (for example, from excess spread), the Company repays the R&W providers. See the section "Breaches of Representations and Warranties" for information about the R&W agreements and eligible assets held in trust with respect to such agreements. When the Company projects receiving more reimbursements in the future than it projects paying in claims on transactions covered by R&W settlement agreements, the Company will have a net R&W payable.

The following tables present the present value of net expected loss to be paid for all contracts by accounting model, by sector and after the benefit for expected recoveries for breaches of R&W.

Net Expected Loss to be Paid (Recovered)
By Accounting Model
As of June 30, 2016

	Financial Guaranty Insurance	FG VIEs(1) and Other	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$963	$ —	$ 0	$963
Non-U.S. public finance	37	—	—	37
Public Finance	1,000	—	0	1,000
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	3	—	—	3
Alt-A first lien	(115)	20	(1)	(96)
Option ARM	(51)	—	(5)	(56)
Subprime	145	50	32	227
Total first lien	(18)	70	26	78
Second lien	68	43	3	114
Total U.S. RMBS	50	113	29	192
Triple-X life insurance transactions	89	—	11	100
Student loans	31	—	—	31
Other structured finance	38	1	(36)	3
Structured Finance	208	114	4	326

Total	$1,208	$ 114	$ 4	$1,326

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Net Expected Loss to be Paid (Recovered)
By Accounting Model
As of December 31, 2015

	Financial Guaranty Insurance	FG VIEs(1) and Other	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$771	$ —	$ 0	$771
Non-U.S. public finance	38	—	—	38
Public Finance	809	—	0	809
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	2	—	(4)	(2)
Alt-A first lien	110	17	0	127
Option ARM	(27)	—	(1)	(28)
Subprime	153	59	39	251
Total first lien	238	76	34	348
Second lien	13	44	4	61
Total U.S. RMBS	251	120	38	409
Triple-X life insurance transactions	88	—	11	99
Student loans	54	—	—	54
Other structured finance	37	16	(33)	20
Structured Finance	430	136	16	582
Total	$1,239	$ 136	$ 16	$1,391

(1) Refer to Note 9, Consolidated Variable Interest Entities.

(2) Refer to Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives.

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The following tables present the net economic loss development for all contracts by accounting model, by sector and after the benefit for expected recoveries for breaches of R&W.

Net Economic Loss Development (Benefit)
By Accounting Model
Second Quarter 2016

	Financial Guaranty Insurance	FG VIEs(1) and Other	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$111	$ —	$ —	$111
Non-U.S. public finance	(2)	—	—	(2)
Public Finance	109	—	—	109
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	0	—	0	0
Alt-A first lien	(39)	2	(1)	(38)
Option ARM	(9)	—	(1)	(10)
Subprime	(17)	(2)	(7)	(26)
Total first lien	(65)	0	(9)	(74)
Second lien	(1)	(6)	0	(7)
Total U.S. RMBS	(66)	(6)	(9)	(81)
Triple-X life insurance transactions	(1)	—	(1)	(2)
Student loans	(1)	—	—	(1)
Other structured finance	(1)	(1)	(1)	(3)
Structured Finance	(69)	(7)	(11)	(87)
Total	$40	$ (7)	$ (11)	$22

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Net Economic Loss Development (Benefit)
By Accounting Model
Second Quarter 2015

	Financial Guaranty Insurance	FG VIEs(1) and Other	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$232	$ —	$ (6)	$226
Non-U.S. public finance	(2)	—	—	(2)
Public Finance	230	—	(6)	224
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	(1)	—	—	(1)
Alt-A first lien	(12)	(1)	(3)	(16)
Option ARM	(4)	—	1	(3)
Subprime	—	(1)	(5)	(6)
Total first lien	(17)	(2)	(7)	(26)
Second lien	(7)	—	1	(6)
Total U.S. RMBS	(24)	(2)	(6)	(32)
Triple-X life insurance transactions	1	—	1	2
Student loans	1	—	—	1
Other structured finance	(1)	1	(3)	(3)
Structured Finance	(23)	(1)	(8)	(32)
Total	$207	$ (1)	$ (14)	$192

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Net Economic Loss Development (Benefit)
By Accounting Model
Six Months 2016

	Financial Guaranty Insurance	FG VIEs(1) and Other	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$209	$ —	$ —	$209
Non-U.S. public finance	(1)	—	—	(1)
Public Finance	208	—	—	208
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	0	—	0	0
Alt-A first lien	(56)	3	(1)	(54)
Option ARM	(28)	—	(3)	(31)
Subprime	(14)	(2)	(9)	(25)
Total first lien	(98)	1	(13)	(110)
Second lien	1	(3)	0	(2)
Total U.S. RMBS	(97)	(2)	(13)	(112)
Triple-X life insurance transactions	2	—	0	2
Student loans	(15)	—	—	(15)
Other structured finance	3	(1)	(4)	(2)
Structured Finance	(107)	(3)	(17)	(127)
Total	$101	$ (3)	$ (17)	$81

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Net Economic Loss Development (Benefit)
By Accounting Model
Six Months 2015

	Financial Guaranty Insurance	FG VIEs(1) and Other	Credit Derivatives(2)	Total
	(in millions)			
Public Finance:				
U.S. public finance	$241	$ —	$ (6)	$235
Non-U.S. public finance	(5)	—	—	(5)
Public Finance	236	—	(6)	230
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	0	—	(1)	(1)
Alt-A first lien	(10)	(1)	(10)	(21)
Option ARM	(3)	—	4	1
Subprime	(4)	3	(6)	(7)
Total first lien	(17)	2	(13)	(28)
Second lien	1	(1)	—	—
Total U.S. RMBS	(16)	1	(13)	(28)
Triple-X life insurance transactions	5	—	2	7
Student loans	(5)	—	—	(5)
Other structured finance	(1)	—	(14)	(15)
Structured Finance	(17)	1	(25)	(41)
Total	$219	$ 1	$ (31)	$189

(1) Refer to Note 9, Consolidated Variable Interest Entities.

(2) Refer to Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives.

Selected U.S. Public Finance Transactions

The Company insures general obligation bonds of the Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations aggregating $5.1 billion net par as of June 30, 2016, all of which are BIG. For additional information regarding the Company's exposure to general obligations of Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations, please refer to "Exposure to Puerto Rico" in Note 4, Outstanding Exposure.

On February 25, 2015, a plan of adjustment resolving the bankruptcy filing of the City of Stockton, California under chapter 9 of the U.S. Bankruptcy Code became effective. As of June 30, 2016, the Company’s net par subject to the plan consists of $115 million of pension obligation bonds. As part of the plan settlement, the City will repay the pension obligation bonds from certain fixed payments and certain variable payments contingent on the City's revenue growth.

The Company has approximately $20 million of net par exposure as of June 30, 2016 to bonds issued by Parkway East Public Improvement District, which is located in Madison County, Mississippi. The bonds, which are rated BIG, are payable from special assessments on properties within the District, as well as amounts paid under a contribution

agreement with the County in which the County covenants that it will provide funds in the event special assessments are not sufficient to make a debt service payment. The special assessments have not been sufficient to pay debt service in full. In earlier years, the County provided funding to cover the balance of the debt service requirement, but the County now claims that the District’s failure to

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reimburse it within the two years stipulated in the contribution agreement means that the County is not required to provide funding until it is reimbursed. On April 27, 2016, the court granted the Company's motion for summary judgment in a declaratory judgment action, agreeing with the Company's interpretation of the County's obligations under the contribution agreement. See "Recovery Litigation" below.

The Company also has $13.6 billion of net par exposure to healthcare transactions. The BIG net par outstanding in this sector is $303 million.

The Company projects that its total net expected loss across its troubled U.S. public finance credits as of June 30, 2016, which incorporated the likelihood of the various outcomes, will be $963 million, compared with a net expected loss of $771 million as of December 31, 2015. Economic loss development in Second Quarter 2016 and Six Months 2016 was $111 million and $209 million, respectively, which was primarily attributable to Puerto Rico exposures.

Certain Selected European Country Sub-Sovereign Transactions

The Company insures and reinsures credits with sub-sovereign exposure to various Spanish and Portuguese issuers where a Spanish and Portuguese sovereign default may cause the sub-sovereigns also to default. The Company's exposure net of reinsurance to these Spanish and Portuguese credits is $366 million and $80 million, respectively. The Company rates most of these issuers in the BB category due to the financial condition of Spain and Portugal and their dependence on the sovereign. The Company's Hungary exposure is to infrastructure bonds dependent on payments from Hungarian governmental entities. The Company's exposure net of reinsurance to these Hungarian credits is $265 million, all of which is rated BIG. The Company estimated net expected losses of $34 million related to these Spanish, Portuguese and Hungarian credits. The economic benefit of approximately $2 million during Second Quarter 2016 and approximately $1 million during Six Months 2016 was primarily related to changes in the exchange rate between the Euro and U.S. Dollar.

Approach to Projecting Losses in U.S. RMBS

The Company projects losses on its insured U.S. RMBS on a transaction-by-transaction basis by projecting the performance of the underlying pool of mortgages over time and then applying the structural features (i.e., payment priorities and tranching) of the RMBS and any R&W agreements to the projected performance of the collateral over time. The resulting projected claim payments or reimbursements are then discounted using risk-free rates.

Second Quarter 2016 U.S. RMBS Loss Projections

Based on its observation during the period of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and loss severity) as well as the residential property market and economy in general, the Company chose to use the same general assumptions to project RMBS losses as of June 30, 2016 as it used as of December 31, 2015, but increased severities for specific vintages of Alt-A first lien and Option ARM transactions, decreased liquidation rates for certain vintages of subprime and increased liquidation rates for second lien transactions based on observed data.

U.S. First Lien RMBS Loss Projections: Alt-A First Lien, Option ARM, Subprime and Prime

The majority of projected losses in first lien RMBS transactions are expected to come from non-performing mortgage loans (those that are or in the past twelve months have been two or more payments behind, have been modified, are in foreclosure, or have been foreclosed upon). Changes in the amount of non-performing loans from the amount projected in the previous period are one of the primary drivers of loss development in this portfolio. In order to determine the number of defaults resulting from these delinquent and foreclosed loans, the Company applies a

liquidation rate assumption to loans in each of various non-performing categories. The Company arrived at its liquidation rates based on data purchased from a third party provider and assumptions about how delays in the foreclosure process and loan modifications may ultimately affect the rate at which loans are liquidated. Each quarter the Company reviews the most recent twelve months of this data and (if necessary) adjusts its liquidation rates based on its observations. The following table shows liquidation assumptions for various non-performing categories.

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First Lien Liquidation Rates

	June 30, 2016	March 31, 2016	December 31, 2015
Current Loans Modified in the Previous 12 Months			
Alt A and Prime	25%	25%	25%
Option ARM	25	25	25
Subprime	25	25	25
Current Loans Delinquent in the Previous 12 Months			
Alt A and Prime	25	25	25
Option ARM	25	25	25
Subprime	25	25	25
30 – 59 Days Delinquent			
Alt A and Prime	35	35	35
Option ARM	40	40	40
Subprime	45	45	45
60 – 89 Days Delinquent			
Alt A and Prime	45	45	45
Option ARM	50	50	50
Subprime	50	55	55
90+ Days Delinquent			
Alt A and Prime	55	55	55
Option ARM	60	60	60
Subprime	55	60	60
Bankruptcy			
Alt A and Prime	45	45	45
Option ARM	50	50	50
Subprime	40	40	40
Foreclosure			
Alt A and Prime	65	65	65
Option ARM	70	70	70
Subprime	65	70	70
Real Estate Owned			
All	100	100	100

While the Company uses liquidation rates as described above to project defaults of non-performing loans (including current loans modified or delinquent within the last 12 months), it projects defaults on presently current loans by applying a conditional default rate ("CDR") trend. The start of that CDR trend is based on the defaults the Company projects will emerge from currently nonperforming, recently nonperforming and modified loans. The total amount of expected defaults from the non-performing loans is translated into a constant CDR (i.e., the CDR plateau), which, if applied for each of the next 36 months, would be sufficient to produce approximately the amount of defaults that were calculated to emerge from the various delinquency categories. The CDR thus calculated individually on the delinquent collateral pool for each RMBS is then used as the starting point for the CDR curve used to project defaults of the presently performing loans.

In the base case, after the initial 36-month CDR plateau period, each transaction’s CDR is projected to improve over 12 months to an intermediate CDR (calculated as 20% of its CDR plateau); that intermediate CDR is held constant for 36 months and then trails off in steps to a final CDR of 5% of the CDR plateau. In the base case, the Company assumes the final CDR will be reached 7 years after the initial 36-month CDR plateau period. Under the Company’s methodology, defaults projected to occur in the first 36 months represent defaults that can be attributed to loans that

were modified or delinquent in the last 12 months or that are currently delinquent or in foreclosure, while the defaults projected to occur using the projected CDR trend after the first 36 month period represent defaults attributable to borrowers that are currently performing or are projected to reperform.

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Another important driver of loss projections is loss severity, which is the amount of loss the transaction incurs on a loan after the application of net proceeds from the disposal of the underlying property. Loss severities experienced in first lien transactions have reached historically high levels, and the Company is assuming in the base case that these high levels generally will continue for another 18 months. The Company determines its initial loss severity based on actual recent experience. As a result, as of March 31, 2016, the Company updated severities for specific vintages of Alt-A first lien and subprime transactions based on observed data and as of June 30, 2016 the Company updated severities again for certain vintages of Alt-A, as well as Option ARM. The Company then assumes that loss severities begin returning to levels consistent with underwriting assumptions beginning after the initial 18 month period, declining to 40% in the base case over 2.5 years.

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The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions used in the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 first lien U.S. RMBS.

Key Assumptions in Base Case Expected Loss Estimates
First Lien RMBS(1)

	As of June 30, 2016		As of March 31, 2016		As of December 31, 2015	
	Range	Weighted Average	Range	Weighted Average	Range	Weighted Average
Alt-A First Lien						
Plateau CDR	0.9%-27.0%	6.1%	0.9%-27.8%	6.4%	1.7%–26.4%	6.4%
Intermediate CDR	0.2%-5.4%	1.2%	0.2%-5.6%	1.3%	0.3%–5.3%	1.3%
Period until intermediate CDR	48 months		48 months		48 months	
Final CDR	0.0%-1.3%	0.3%	0.0%-1.4%	0.3%	0.1%–1.3%	0.3%
Initial loss severity:						
2005 and prior	60.0%		60.0%		60.0%	
2006	80.0%		80.0%		70.0%	
2007	70.0%		65.0%		65.0%	
Initial conditional prepayment rate ("CPR")	3.5%-29.3%	11.0%	2.7%-31.6%	11.8%	2.7%–32.5%	11.5%
Final CPR(2)	15%		15%		15%	
Option ARM						
Plateau CDR	3.2%-10.1%	7.4%	3.4%-10.6%	7.8%	3.5%–10.3%	7.8%
Intermediate CDR	0.6%-2.0%	1.5%	0.7%-2.1%	1.6%	0.7%–2.1%	1.6%
Period until intermediate CDR	48 months		48 months		48 months	
Final CDR	0.2%-0.5%	0.3%	0.2%-0.5%	0.4%	0.2%–0.5%	0.4%
Initial loss severity:						
2005 and prior	60.0%		60.0%		60.0%	
2006	70.0%		70.0%		70.0%	
2007	75.0%		65.0%		65.0%	
Initial CPR	2.0%-13.2%	5.7%	2.0%-13.7%	5.5%	1.5%–10.9%	5.1%
Final CPR(2)	15%		15%		15%	
Subprime						
Plateau CDR	4.4%-12.7%	8.5%	4.2%-14.4%	9.4%	4.7%–13.2%	9.5%
Intermediate CDR	0.9%-2.5%	1.7%	0.8%-2.9%	1.9%	0.9%–2.6%	1.9%
Period until intermediate CDR	48 months		48 months		48 months	
Final CDR	0.2%-0.6%	0.4%	0.2%-0.7%	0.4%	0.2%–0.7%	0.4%
Initial loss severity:						
2005 and prior	80.0%		80.0%		75.0%	
2006	90.0%		90.0%		90.0%	
2007	90.0%		90.0%		90.0%	
Initial CPR	0.6%-11.3%	4.9%	0.3%-9.2%	4.2%	0.0%–10.1%	3.6%
Final CPR(2)	15%		15%		15%	

(1) Represents variables for most heavily weighted scenario (the “base case”).

(2) For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used.

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The rate at which the principal amount of loans is voluntarily prepaid may impact both the amount of losses projected (since that amount is a function of the CDR, the loss severity and the loan balance over time) as well as the amount of excess spread (the amount by which the interest paid by the borrowers on the underlying loan exceeds the amount of interest owed on the insured obligations). The assumption for the voluntary CPR follows a similar pattern to that of the CDR. The current level of voluntary prepayments is assumed to continue for the plateau period before gradually increasing over 12 months to the final CPR, which is assumed to be 15% in the base case. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. These CPR assumptions are the same as those the Company used for March 31, 2016 and December 31, 2015.

In estimating expected losses, the Company modeled and probability weighted sensitivities for first lien transactions by varying its assumptions of how fast a recovery is expected to occur. One of the variables used to model sensitivities was how quickly the CDR returned to its modeled equilibrium, which was defined as 5% of the initial CDR. The Company also stressed CPR and the speed of recovery of loss severity rates. The Company probability weighted a total of five scenarios as of June 30, 2016. The Company used a similar approach to establish its pessimistic and optimistic scenarios as of June 30, 2016 as it used as of March 31, 2016 and December 31, 2015, increasing and decreasing the periods of stress from those used in the base case.

In a somewhat more stressful environment than that of the base case, where the CDR plateau was extended six months (to be 42 months long) before the same more gradual CDR recovery and loss severities were assumed to recover over 4.5 rather than 2.5 years (and subprime loss severities were assumed to recover only to 60% and Option ARM and Alt A loss severities to only 45%), expected loss to be paid would increase from current projections by approximately $13 million for Alt-A first liens, $7 million for Option ARM, $43 million for subprime and $0.1 million for prime transactions.

In an even more stressful scenario where loss severities were assumed to rise and then recover over nine years and the initial ramp-down of the CDR was assumed to occur over 15 months and other assumptions were the same as the other stress scenario, expected loss to be paid would increase from current projections by approximately $33 million for Alt-A first liens, $14 million for Option ARM, $59 million for subprime and $0.4 million for prime transactions.

In a scenario with a somewhat less stressful environment than the base case, where CDR recovery was somewhat less gradual, expected loss to be paid would decrease from current projections by approximately $6 million for Alt-A first liens, $21 million for Option ARM, $10 million for subprime and $17 thousand for prime transactions.

In an even less stressful scenario where the CDR plateau was six months shorter (30 months, effectively assuming that liquidation rates would improve) and the CDR recovery was more pronounced (including an initial ramp-down of the CDR over nine months), expected loss to be paid would decrease from current projections by approximately $18 million for Alt-A first liens, $32 million for Option ARM, $35 million for subprime and $0.1 million for prime transactions.

U.S. Second Lien RMBS Loss Projections

Second lien RMBS transactions include both home equity lines of credit ("HELOC") and closed end second lien. The Company believes the primary variable affecting its expected losses in second lien RMBS transactions is the amount and timing of future losses in the collateral pool supporting the transactions. Expected losses are also a function of the structure of the transaction; the voluntary prepayment rate (typically also referred to as CPR of the collateral); the interest rate environment; and assumptions about the draw rate and loss severity.

In second lien transactions the projection of near-term defaults from currently delinquent loans is relatively straightforward because loans in second lien transactions are generally “charged off” (treated as defaulted) by the

securitization’s servicer once the loan is 180 days past due. The Company estimates the amount of loans that will default over the next six months by calculating current representative liquidation rates. A liquidation rate is the percent of loans in a given cohort (in this instance, delinquency category) that ultimately default. Similar to first liens, the Company then calculates a CDR for six months, which is the period over which the currently delinquent collateral is expected to be liquidated. That CDR is then used as the basis for the plateau CDR period that follows the embedded five months of losses. Liquidation rates assumed as of June 30, 2016 were from 25% to 100%, which were the same as of March 31, 2016. Liquidation rates assumed as of December 31, 2015 were from 10% to 100%.

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For the base case scenario, the CDR (the “plateau CDR”) was held constant for six months. Once the plateau period has ended, the CDR is assumed to gradually trend down in uniform increments to its final long-term steady state CDR. (The long-term steady state CDR is calculated as the constant CDR that would have yielded the amount of losses originally expected at underwriting.) In the base case scenario, the time over which the CDR trends down to its final CDR is 28 months. Therefore, the total stress period for second lien transactions is 34 months, comprising five months of delinquent data, a one month plateau period and 28 months of decrease to the steady state CDR, the same as of March 31, 2016 and December 31, 2015.

HELOC loans generally permit the borrower to pay only interest for an initial period (often ten years) and, after that period, require the borrower to make both the monthly interest payment and a monthly principal payment, and so increase the borrower's aggregate monthly payment. Some of the HELOC loans underlying the Company's insured HELOC transactions have reached their principal amortization period. The Company has observed that the increase in monthly payments occurring when a loan reaches its principal amortization period, even if mitigated by borrower relief offered by the servicer, is associated with increased borrower defaults. Thus, most of the Company's HELOC projections incorporate an assumption that a percentage of loans reaching their amortization periods will default around the time of the payment increase. These projected defaults are in addition to those generated using the CDR curve as described above. This assumption is similar to the one used as of March 31, 2016 and December 31, 2015. For June 30, 2016 the Company used the same general approach as of March 31, 2016 and December 31, 2015.

When a second lien loan defaults, there is generally a very low recovery. The Company had assumed as of June 30, 2016 that it will generally recover only 2% of the collateral defaulting in the future and declining additional amounts of post-default receipts on previously defaulted collateral. This is the same assumption used as of March 31, 2016 and December 31, 2015.

The rate at which the principal amount of loans is prepaid may impact both the amount of losses projected as well as the amount of excess spread. In the base case, an average CPR (based on experience of the past year) is assumed to continue until the end of the plateau before gradually increasing to the final CPR over the same period the CDR decreases. The final CPR is assumed to be 15% for second lien transactions, which is lower than the historical average but reflects the Company’s continued uncertainty about the projected performance of the borrowers in these transactions. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. This pattern is generally consistent with how the Company modeled the CPR as of March 31, 2016 and December 31, 2015. To the extent that prepayments differ from projected levels it could materially change the Company’s projected excess spread and losses.

The Company uses a number of other variables in its second lien loss projections, including the spread between relevant interest rate indices. These variables have been relatively stable and in the relevant ranges have less impact on the projection results than the variables discussed above. However, in a number of HELOC transactions the servicers have been modifying poorly performing loans from floating to fixed rates, and, as a result, rising interest rates would negatively impact the excess spread available from these modified loans to support the transactions. The Company incorporated these modifications in its assumptions.

In estimating expected losses, the Company modeled and probability weighted five possible CDR curves applicable to the period preceding the return to the long-term steady state CDR. The Company used five scenarios at June 30, 2016 and December 31, 2015. The Company believes that the level of the elevated CDR and the length of time it will persist, the ultimate prepayment rate, and the amount of additional defaults because of the expiry of the interest only period, are the primary drivers behind the likely amount of losses the collateral will suffer. The Company continues to evaluate the assumptions affecting its modeling results.

Most of the Company's projected second lien RMBS losses are from HELOC transactions. The following table shows the range as well as the average, weighted by outstanding net insured par, for key assumptions for the calculation of expected loss to be paid for individual transactions for direct vintage 2004 - 2008 HELOCs.

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Key Assumptions in Base Case Expected Loss Estimates
HELOCs (1)

	As of June 30, 2016		As of March 31, 2016		As of December 31, 2015	
	Range	Weighted Average	Range	Weighted Average	Range	Weighted Average
Plateau CDR	2.5 %–26.3%	12.6%	5.3 %–26.1%	11.9%	4.9 %–23.5%	10.3%
Final CDR trended down to	0.5 %–3.2%	1.2%	0.5 %–3.2%	1.2%	0.5 %–3.2%	1.2%
Period until final CDR	34 months		34 months		34 months	
Initial CPR	11.0%–15.4%	11.1%	11.0%–14.9%	11.1%	10.9%	
Final CPR(2)	10.0%–15.4%	13.3%	10.0%–15.0%	13.3%	10.0%–15.0%	13.3%
Loss severity	98.0%		98.0%		98.0%	

(1) Represents variables for most heavily weighted scenario (the “base case”).

(2) For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used.

The Company’s base case assumed a six month CDR plateau and a 28 month ramp-down (for a total stress period of 34 months). The Company also modeled a scenario with a longer period of elevated defaults and another with a shorter period of elevated defaults. Increasing the CDR plateau to eight months and increasing the ramp-down by three months to 31 months (for a total stress period of 39 months), and doubling the defaults relating to the end of the interest only period would increase the expected loss by approximately $49 million for HELOC transactions. On the other hand, reducing the CDR plateau to four months and decreasing the length of the CDR ramp-down to 25 months (for a total stress period of 29 months), and lowering the ultimate prepayment rate to 10% would decrease the expected loss by approximately $30 million for HELOC transactions.

Breaches of Representations and Warranties

The Company entered into agreements with R&W providers under which those providers made payments to the Company, agreed to make payments to the Company in the future, and / or repurchased loans from the transactions, all in return for releases of related liability by the Company.

As of June 30, 2016, the Company had a net R&W payable of $58 million to R&W counterparties, compared to an R&W recoverable of $79 million as of December 31, 2015. The decrease represents improvements in underlying collateral performance and the termination of the Deutsche Bank agreement described below. The Company’s agreements with providers of R&W generally provide for reimbursement to the Company as claim payments are made and, to the extent the Company later receives reimbursements of such claims from excess spread or other sources, for the Company to provide reimbursement to the R&W providers. When the Company projects receiving more reimbursements in the future than it projects to pay in claims on transactions covered by R&W settlement agreements, the Company will have a net R&W payable. Most of the amount projected to be received pursuant to agreements with R&W providers benefits from eligible assets placed in trusts to collateralize the R&W provider’s future reimbursement obligation, with the amount of such collateral subject to increase or decrease from time to time as determined by rating agency requirements. Currently the Company has agreements with two counterparties where a future reimbursement obligation is collateralized by eligible assets held in trust:

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Bank of America. Under the Company's agreement with Bank of America Corporation and certain of its subsidiaries (“Bank of America”), Bank of America agreed to reimburse the Company for 80% of claims on the first lien transactions covered by the agreement that the Company pays in the future, until the aggregate lifetime collateral losses (not insurance losses or claims) on those transactions reach $6.6 billion. As of June 30, 2016 aggregate lifetime collateral losses on those transactions was $4.5 billion, and the Company was projecting in its base case that such collateral losses would eventually reach $5.2 billion. Bank of America's reimbursement obligation is secured by $577 million of collateral held in trust for the Company's benefit.

- UBS. Under the Company’s agreement with UBS Real Estate Securities Inc. and affiliates (“UBS”), UBS agreed to reimburse the Company for 85% of future losses on three first lien RMBS transactions, and such reimbursement obligation is secured by $44 million of collateral held in trust for the Company's benefit.

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Under the Company's previous agreement with Deutsche Bank AG and certain of its affiliates (collectively, “Deutsche Bank”), Deutsche Bank agreed to reimburse the Company for certain claims it pays in the future on eight first and second lien transactions, including 80% of claims it pays on those transactions until the aggregate lifetime claims (before reimbursement) reach $319 million. In May 2016, Deutsche Bank's reimbursement obligations under the May 2012 agreement were terminated in return for cash payments to the Company.

The Company uses the same RMBS projection scenarios and weightings to project its future R&W benefit as it uses to project RMBS losses on its portfolio. To the extent the Company increases its loss projections, the R&W benefit generally will also increase, subject to the agreement limits and thresholds described above. Similarly, to the extent the Company decreases its loss projections, the R&W benefit generally will also decrease, subject to the agreement limits and thresholds described above.

Triple-X Life Insurance Transactions

The Company had $2.2 billion of net par exposure to Triple-X life insurance transactions as of June 30, 2016. Two of these transactions, with $216 million of net par outstanding, are rated BIG. The Triple-X life insurance transactions are based on discrete blocks of individual life insurance business. In older vintage Triple-X life insurance transactions, which include the two BIG-rated transactions, the amounts raised by the sale of the notes insured by the Company were used to capitalize a special purpose vehicle that provides reinsurance to a life insurer or reinsurer. The monies are invested at inception in accounts managed by third-party investment managers. In the case of the two BIG-rated transactions, material amounts of their assets were invested in U.S. RMBS. Based on its analysis of the information currently available, including estimates of future investment performance, and projected credit impairments on the invested assets and performance of the blocks of life insurance business at June 30, 2016, the Company’s projected net expected loss to be paid is $100 million. The economic benefit during Second Quarter 2016 was approximately $2 million, which was due primarily to changes in interest rates and updates to the projected asset cash flows. The economic loss development during Six Months 2016 was approximately $2 million, which was due primarily to changes in discount rates and updates to the projected life insurance cash flows.

Student Loan Transactions

The Company has insured or reinsured $1.6 billion net par of student loan securitizations issued by private issuers and that it classifies as structured finance. Of this amount, $110 million is rated BIG. The Company is projecting approximately $31 million of net expected loss to be paid on these transactions. In general, the losses are due to: (i) the poor credit performance of private student loan collateral and high loss severities, or (ii) high interest rates on auction rate securities with respect to which the auctions have failed. The economic benefit during Second Quarter 2016 was approximately $1 million, which was driven primarily by changes in interest rates. The economic benefit during Six Months 2016 was approximately $15 million, which was driven primarily by the commutation of certain assumed student loan exposures earlier in the year.

TruPS and other structured finance

The Company's TruPS sector has BIG par of $563 million and all other structured finance BIG par totaled $828 million, comprising primarily transactions backed by perpetual preferred securities, commercial receivables and manufactured housing loans. The Company has expected loss to be paid of $3 million for TruPS and other structured finance transactions as of June 30, 2016. The economic benefit during Second Quarter 2016 was $3 million, which was attributable primarily to improved performance of various credits. The economic benefit during Six Months 2016 was $2 million, which was attributable primarily to improved performance of various credits.

Recovery Litigation

Public Finance Transactions

On January 7, 2016, AGM, AGC and Ambac Assurance Corporation (“Ambac”) commenced an action for declaratory judgment and injunctive relief in the U.S. District Court for the District of Puerto Rico to invalidate the executive orders issued by the Governor on November 30, 2015 and December 8, 2015 directing that the Secretary of the Treasury of the Commonwealth of Puerto Rico and the Puerto Rico Tourism Company retain or transfer (in other words, "claw back") certain taxes and revenues pledged to secure the payment of bonds issued by the Puerto Rico Highways and Transportation Authority, the Puerto Rico Convention Center District Authority and the Puerto Rico Infrastructure Financing Authority. The action is still in its early stages.

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On July 21, 2016, AGC and AGM filed a motion and form of complaint in the U.S. District Court for the District of Puerto Rico seeking relief from the stay provided by PROMESA. Upon a grant of relief from the PROMESA stay, the lawsuit further seeks a declaration that the Moratorium Act is preempted by Federal bankruptcy law and that certain gubernatorial executive orders diverting PRHTA pledged toll revenues (which are not subject to the Clawback) are preempted by PROMESA and violate the U.S. Constitution. Additionally, it seeks damages for the value of the PRHTA toll revenues diverted and injunctive relief prohibiting the defendants from taking any further action under these executive orders.

On November 1, 2013, Radian Asset commenced a declaratory judgment action in the U.S. District Court for the Southern District of Mississippi against Madison County, Mississippi and the Parkway East Public Improvement District to establish its rights under a contribution agreement from the County supporting certain special assessment bonds issued by the District and insured by Radian Asset (now AGC). As of June 30, 2016, $20 million of such bonds were outstanding. The County maintained that its payment obligation is limited to two years of annual debt service, while AGC contended the County’s obligations under the contribution agreement continue so long as the bonds remain outstanding. On April 27, 2016, the Court granted AGC's motion for summary judgment, agreeing with AGC's interpretation of the County's obligations. On May 11, 2016, the County filed a notice of appeal of that ruling to the United States Court for the Fifth Circuit.

Triple-X Life Insurance Transactions

In December 2008 AGUK filed an action in the Supreme Court of the State of New York against J.P. Morgan Investment Management Inc. (“JPMIM”), the investment manager for a triple-X life insurance transaction, Orkney Re II plc ("Orkney"), involving securities guaranteed by AGUK. The action alleges that JPMIM engaged in breaches of fiduciary duty, gross negligence and breaches of contract based upon its handling of the Orkney investments. After AGUK’s claims were dismissed with prejudice in January 2010, AGUK was successful in its subsequent motions and appeals and, as of December 2011, all of AGUK’s claims for breaches of fiduciary duty, gross negligence and contract were reinstated in full. On January 22, 2016, AGUK filed a motion for partial summary judgment with respect to one of its claims for breach of contract relating to a failure to invest in compliance with the Delaware insurance code. Discovery was completed on February 22, 2016, and oral argument on the motion for partial summary judgment is scheduled for August 2016.

RMBS Transactions

On February 5, 2009, U.S. Bank National Association, as indenture trustee ("U.S. Bank”), CIFG, as insurer of the Class Ac Notes, and Syncora Guarantee Inc. ("Syncora"), as insurer of the Class Ax Notes, filed a complaint in the Supreme Court of the State of New York against GreenPoint Mortgage Funding, Inc. ("GreenPoint") alleging GreenPoint breached its representations and warranties with respect to the underlying mortgage loans in the GreenPoint Mortgage Funding Trust 2006-HE1 transaction. On March 3, 2010, the court dismissed CIFG's and Syncora’s causes of action on standing grounds. On December 16, 2013, GreenPoint moved to dismiss the remaining claims of U.S. Bank on the grounds that it too lacked standing. U.S. Bank cross-moved for partial summary judgment striking GreenPoint’s defense that U.S. Bank lacked standing to directly pursue claims against GreenPoint. On January 28, 2016, the court denied GreenPoint’s motion for summary judgment and granted U.S. Bank’s cross-motion for partial summary judgment, finding that as a matter of law U.S. Bank has standing to directly assert claims against GreenPoint. On February 26, 2016, GreenPoint filed a notice of appeal of that decision but to date has not perfected its appeal.

On November 26, 2012, CIFG filed a complaint in the Supreme Court of the State of New York against JP Morgan Securities LLC ("JP Morgan") for material misrepresentation in the inducement of insurance and common law fraud, alleging that JP Morgan fraudulently induced CIFG to insure $400 million of securities issued by ACA ABS CDO 2006-2 Ltd. and $325 million of securities issued by Libertas Preferred Funding II, Ltd. On June 26, 2015, the Court

dismissed with prejudice CIFG’s material misrepresentation in the inducement of insurance claim and dismissed without prejudice CIFG’s common law fraud claim. On September 24, 2015, the Court denied CIFG’s motion to amend but allowed CIFG to re-plead a cause of action for common law fraud. On November 20, 2015, CIFG filed a motion for leave to amend its complaint to re-plead common law fraud. On April 29, 2016, CIFG filed an appeal to reverse the Court’s decision dismissing CIFG’s material misrepresentation in the inducement of insurance claim.

On January 15, 2013, CIFG filed a complaint in the Supreme Court of the State of New York against Goldman, Sachs & Co. ("Goldman") for material misrepresentation in the inducement of insurance and common law fraud, alleging that Goldman fraudulently induced CIFG to insure $325 million of Class A-1 Notes (the “Class A-1 Notes”) and to purchase $10 million of Class A-2 Notes (the “Class A-2 Notes”) issued by Fortius II Funding, Ltd. CDO. CIFG and Goldman agreed to separately arbitrate the issue of liability with respect to CIFG’s purchase of the Class A-2 Notes, and on February 4, 2015, an arbitration panel awarded CIFG $2.5 million in damages. On September 11, 2015, CIFG filed an amended complaint to allege

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that the arbitration award collaterally estopped Goldman from disputing its liability for fraudulent inducement in respect of the Class A-1 Notes. On July 7, 2016, the Court heard oral argument on (i) the motion of AGC (as successor to CIFG) for partial summary judgment on the issue of Goldman's liability for material misrepresentation in the inducement of insurance and fraud with respect to the Class A-1 Notes policy and (ii) Goldman's motion to dismiss AGC's amended complaint.

6. Financial Guaranty Insurance

Financial Guaranty Insurance Premiums

The portfolio of outstanding exposures discussed in Note 4, Outstanding Exposure, includes financial guaranty contracts that meet the definition of insurance contracts as well as those that meet the definition of a derivative under GAAP. Amounts presented in this note relate to financial guaranty insurance contracts, unless otherwise noted. See Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives for amounts that relate to CDS and Note 9, Consolidated Variable Interest Entities for amounts that relate to FG VIEs.

Net Earned Premiums

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Scheduled net earned premiums	$93	$118	$184	$214
Acceleration of net earned premiums (1)	117	96	206	137
Accretion of discount on net premiums receivable	4	5	7	9
Financial guaranty insurance net earned premiums	214	219	397	360
Other	—	0	0	1
Net earned premiums (2)	$214	$219	$397	$361

(1) Reflects the unscheduled refunding or termination of the insurance on an insured obligation as well as changes in scheduled earnings due to changes in the expected lives of the insured obligations.

(2) Excludes $3 million and $5 million for Second Quarter 2016 and 2015, respectively, and $8 million and $10 million for Six Months 2016 and 2015, respectively, related to consolidated FG VIEs.

Components of Unearned Premium Reserve

	As of June 30, 2016			As of December 31, 2015		
	Gross	Ceded	Net(1)	Gross	Ceded	Net(1)
	(in millions)					
Deferred premium revenue	3,641	230	3,411	4,008	238	3,770
Contra-paid (2)	(24)	(2)	(22)	(12)	(6)	(6)
Unearned premium reserve	$3,617	$228	$3,389	$3,996	$232	$3,764

(1) Excludes $98 million and $110 million of deferred premium revenue, and $30 million and $30 million of contra-paid related to FG VIEs as of June 30, 2016 and December 31, 2015, respectively.

(2) See "Financial Guaranty Insurance Losses– Insurance Contracts' Loss Information" below for an explanation of "contra-paid".

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Gross Premium Receivable,
Net of Commissions on Assumed Business
Roll Forward

	Six Months	
	2016	2015
	(in millions)	
Beginning of period, December 31	$693	$729
Premiums receivable acquired in Radian Asset Acquisition on April 1, 2015	—	2
Gross written premiums, net of commissions on assumed business	83	61
Gross premiums received, net of commissions on assumed business	(107)	(79)
Adjustments:		
Changes in the expected term	(27)	(9)
Accretion of discount, net of commissions on assumed business	3	10
Foreign exchange translation	(22)	(8)
Consolidation/deconsolidation of FG VIEs	0	(4)
End of period, June 30 (1)	$623	$702

(1) Excludes $11 million and $23 million as of June 30, 2016 and June 30, 2015, respectively, related to consolidated FG VIEs. Excludes $1 million related to non-financial guaranty line of business as of June 30, 2015.

Foreign exchange translation relates to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 55%, 52% and 50% of installment premiums at June 30, 2016, December 31, 2015 and June 30, 2015, respectively, are denominated in currencies other than the U.S. dollar, primarily the Euro and British Pound Sterling.

The timing and cumulative amount of actual collections may differ from expected collections in the tables below due to factors such as foreign exchange rate fluctuations, counterparty collectability issues, accelerations, commutations and changes in expected lives.

Expected Collections of
Financial Guaranty Insurance Gross Premiums Receivable,
Net of Commissions on Assumed Business
(Undiscounted)

	As of June 30, 2016
	(in millions)
2016 (July 1 – September 30)	$ 21
2016 (October 1 – December 31)	21
2017	66
2018	59
2019	54
2020	53
2021-2025	212
2026-2030	139
2031-2035	97
After 2035	79
Total(1)	$ 801

(1) Excludes expected cash collections on FG VIEs of $14 million.

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Scheduled Financial Guaranty Insurance Net Earned Premiums

	As of June 30, 2016 (in millions)
2016 (July 1 – September 30)	$ 89
2016 (October 1 – December 31)	85
2017	313
2018	287
2019	258
2020	236
2021-2025	922
2026-2030	588
2031-2035	350
After 2035	283
Net deferred premium revenue(1)	3,411
Future accretion	166
Total future net earned premiums	$ 3,577

(1) Excludes scheduled net earned premiums on consolidated FG VIEs of $98 million.

Selected Information for Financial Guaranty Insurance Policies Paid in Installments

	As of June 30, 2016	As of December 31, 2015
	(dollars in millions)	
Premiums receivable, net of commission payable	$ 623	$ 693
Gross deferred premium revenue	1,086	1,240
Weighted-average risk-free rate used to discount premiums	3.1 %	3.1 %
Weighted-average period of premiums receivable (in years)	9.2	9.4

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Financial Guaranty Insurance Losses

Insurance Contracts' Loss Information

The following table provides information on loss and LAE reserves and salvage and subrogation recoverable, net of reinsurance. The Company used weighted average risk-free rates for U.S. dollar denominated financial guaranty insurance obligations that ranged from 0.0% to 2.46% as of June 30, 2016 and 0.0% to 3.25% as of December 31, 2015.

Loss and LAE Reserve and Salvage and Subrogation Recoverable
Net of Reinsurance
Insurance Contracts

	As of June 30, 2016			As of December 31, 2015		
	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net Reserve (Recoverable)
	(in millions)					
Public Finance:						
U.S. public finance	$807	$ 14	$ 793	$604	$ 7	$ 597
Non-U.S. public finance	24	—	24	25	—	25
Public Finance	831	14	817	629	7	622
Structured Finance:						
U.S. RMBS:						
First lien:						
Prime first lien	3	—	3	2	—	2
Alt-A first lien	40	184	(144)	46	—	46
Option ARM	9	58	(49)	13	42	(29)
Subprime	147	14	133	169	21	148
First lien	199	256	(57)	230	63	167
Second lien	84	45	39	32	53	(21)
Total U.S. RMBS	283	301	(18)	262	116	146
Triple-X life insurance transactions	83	—	83	82	—	82
Student loans	30	—	30	51	—	51
Other structured finance	30	1	29	48	—	48
Structured Finance	426	302	124	443	116	327
Subtotal	1,257	316	941	1,072	123	949
Other recoverables	—	3	(3)	—	3	(3)
Subtotal	1,257	319	938	1,072	126	946
Effect of consolidating FG VIEs	(71)	—	(71)	(74)	0	(74)
Total (1)	$1,186	$ 319	$ 867	$998	$ 126	$ 872

(1) See “Components of Net Reserves (Salvage)” table for loss and LAE reserve and salvage and subrogation recoverable components.

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Components of Net Reserves (Salvage)

	As of June 30, 2016	As of December 31, 2015
	(in millions)	
Loss and LAE reserve	$1,268	$ 1,067
Reinsurance recoverable on unpaid losses	(82)	(69)
Loss and LAE reserve, net	1,186	998
Salvage and subrogation recoverable	(323)	(126)
Salvage and subrogation payable(1)	7	3
Other recoverables	(3)	(3)
Salvage and subrogation recoverable, net and other recoverable	(319)	(126)
Net reserves (salvage)	$867	$ 872

(1) Recorded as a component of reinsurance balances payable.

The table below provides a reconciliation of net expected loss to be paid to net expected loss to be expensed. Expected loss to be paid differs from expected loss to be expensed due to: (i) the contra-paid which represent the claim payments made and recoveries received that have not yet been recognized in the statement of operations, (ii) salvage and subrogation recoverable for transactions that are in a net recovery position where the Company has not yet received recoveries on claims previously paid (having the effect of reducing net expected loss to be paid by the amount of the previously paid claim and the expected recovery), but will have no future income effect (because the previously paid claims and the corresponding recovery of those claims will offset in income in future periods), and (iii) loss reserves that have already been established (and therefore expensed but not yet paid).

Reconciliation of Net Expected Loss to be Paid and
Net Expected Loss to be Expensed
Financial Guaranty Insurance Contracts

	As of June 30, 2016
	(in millions)
Net expected loss to be paid - financial guaranty insurance (1)	$ 1,208
Contra-paid, net	22
Salvage and subrogation recoverable, net of reinsurance	316
Loss and LAE reserve - financial guaranty insurance contracts, net of reinsurance	(1,185)
Other recoveries	3
Net expected loss to be expensed (present value) (2)	$ 364

(1) See "Net Expected Loss to be Paid (Recovered) by Accounting Model" table in Note 5, Expected Loss to be Paid.

(2) Excludes $72 million as of June 30, 2016, related to consolidated FG VIEs.

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The following table provides a schedule of the expected timing of net expected losses to be expensed. The amount and timing of actual loss and LAE may differ from the estimates shown below due to factors such as accelerations, commutations, changes in expected lives and updates to loss estimates. This table excludes amounts related to FG VIEs, which are eliminated in consolidation.

Net Expected Loss to be Expensed
Financial Guaranty Insurance Contracts

	As of June 30, 2016 (in millions)
2016 (July 1 – September 30)	$ 9
2016 (October 1 – December 31)	8
Subtotal 2016	17
2017	30
2018	28
2019	29
2020	27
2021-2025	103
2026-2030	71
2031-2035	40
After 2035	19
Net expected loss to be expensed	364
Future accretion	199
Total expected future loss and LAE	$ 563

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The following table presents the loss and LAE recorded in the consolidated statements of operations by sector for insurance contracts. Amounts presented are net of reinsurance.

Loss and LAE
Reported on the
Consolidated Statements of Operations

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Public Finance:				
U.S. public finance	$116	$196	$213	$209
Non-U.S. public finance	(1)	1	(1)	6
Public finance	115	197	212	215
Structured Finance:				
U.S. RMBS:				
First lien:				
Prime first lien	(1)	(1)	(1)	(1)
Alt-A first lien	3	(9)	11	(11)
Option ARM	(7)	0	(21)	(1)
Subprime	(11)	1	(7)	1
First lien	(16)	(9)	(18)	(12)
Second lien	4	0	17	10
Total U.S. RMBS	(12)	(9)	(1)	(2)
Triple-X life insurance transactions	(1)	1	2	7
Student loans	0	1	(14)	(5)
Other structured finance	(3)	0	(3)	(2)
Structured finance	(16)	(7)	(16)	(2)
Loss and LAE on insurance contracts before FG VIE consolidation	99	190	196	213
Effect of consolidating FG VIEs	3	(2)	(4)	(7)
Loss and LAE	$102	$188	$192	$206

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The following table provides information on financial guaranty insurance contracts categorized as BIG.

Financial Guaranty Insurance
BIG Transaction Loss Summary
As of June 30, 2016

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating FG VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	198	(42)	76	(12)	131	(46)	405	—	405
Remaining weighted-average contract period (in years)	9.8	7.4	12.7	10.0	6.6	5.1	10.1	—	10.1
Outstanding exposure:									
Principal	$7,012	$(466)	$4,571	$(452)	$3,276	$(237)	$13,704	$ —	$13,704
Interest	3,618	(200)	2,991	(228)	937	(50)	7,068	—	7,068
Total(2)	$10,630	$(666)	$7,562	$(680)	$4,213	$(287)	$20,772	$ —	$20,772
Expected cash outflows (inflows)	$331	$(27)	$1,466	$(82)	$1,228	$(57)	$2,859	$ (330)	$2,529
Potential recoveries									
Undiscounted R&W	122	(3)	(2)	—	(33)	1	85	—	85
Other(3)	(667)	16	(298)	11	(499)	30	(1,407)	200	(1,207)
Total potential recoveries	(545)	13	(300)	11	(532)	31	(1,322)	200	(1,122)
Subtotal	(214)	(14)	1,166	(71)	696	(26)	1,537	(130)	1,407
Discount	133	(3)	(232)	12	(29)	(97)	(216)	17	(199)
Present value of expected cash flows	$(81)	$(17)	$934	$(59)	$667	$(123)	$1,321	$ (113)	$1,208
Deferred premium revenue	$256	$(8)	$152	$(7)	$347	$(32)	$708	$ (94)	$614
Reserves (salvage)	$(177)	$(11)	$811	$(53)	$378	$(11)	$937	$ (71)	$866

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Financial Guaranty Insurance
BIG Transaction Loss Summary
As of December 31, 2015

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating FG VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	202	(46)	85	(13)	132	(44)	419	—	419
Remaining weighted-average contract period (in years)	10.0	8.7	13.8	9.5	7.7	5.9	10.7	—	10.7
Outstanding exposure:									
Principal	$7,751	$(732)	$3,895	$(240)	$3,087	$(187)	$13,574	$ —	$13,574
Interest	4,109	(354)	2,805	(110)	1,011	(42)	7,419	—	7,419
Total(2)	$11,860	$(1,086)	$6,700	$(350)	$4,098	$(229)	$20,993	$ —	$20,993
Expected cash outflows (inflows)	$386	$(42)	$1,158	$(60)	$1,464	$(53)	$2,853	$ (343)	$2,510
Potential recoveries									
Undiscounted R&W	69	(2)	(49)	1	(85)	5	(61)	7	(54)
Other(3)	(441)	14	(118)	7	(587)	19	(1,106)	175	(931)
Total potential recoveries	(372)	12	(167)	8	(672)	24	(1,167)	182	(985)
Subtotal	14	(30)	991	(52)	792	(29)	1,686	(161)	1,525
Discount	91	3	(286)	12	(58)	(89)	(327)	41	(286)
Present value of expected cash flows	$105	$(27)	$705	$(40)	$734	$(118)	$1,359	$ (120)	$1,239
Deferred premium revenue	$371	$(37)	$150	$(4)	$386	$(32)	$834	$ (100)	$734
Reserves (salvage)	$2	$(19)	$591	$(38)	$404	$(9)	$931	$ (74)	$857

(1) A risk represents the aggregate of the financial guaranty policies that share the same revenue source for purposes of making debt service payments. The ceded number of risks represents the number of risks for which the Company ceded a portion of its exposure.

(2) Includes BIG amounts related to FG VIEs.

(3) Includes excess spread.

Ratings Impact on Financial Guaranty Business

A downgrade of one of AGL's insurance subsidiaries may result in increased claims under financial guaranties issued by the Company, if the insured obligors were unable to pay.

For example, AGM has issued financial guaranty insurance policies in respect of the obligations of municipal obligors under interest rate swaps. AGM insures periodic payments owed by the municipal obligors to the bank counterparties. In certain cases, AGM also insures termination payments that may be owed by the municipal obligors to the bank counterparties. If (i) AGM has been downgraded below the rating trigger set forth in a swap under which it has insured the termination payment, which rating trigger varies on a transaction by transaction basis; (ii) the municipal obligor has the right to cure by, but has failed in, posting collateral, replacing AGM or otherwise curing the downgrade of AGM; (iii) the transaction documents include as a condition that an event of default or termination

event with respect to the municipal obligor has occurred, such as the rating of the municipal obligor being downgraded past a specified level, and such condition has been met; (iv) the bank counterparty has elected to terminate the swap; (v) a termination payment is payable by the municipal obligor; and (vi) the municipal obligor has failed to make the termination payment payable by it, then AGM would be required to pay the termination payment due by the municipal obligor, in an amount not to exceed the policy limit set forth in the financial guaranty insurance policy. At AGM's current financial strength ratings, if the conditions giving rise to the obligation of AGM to make a termination payment under the swap termination policies were all satisfied, then AGM could pay claims in an amount not exceeding approximately $193 million in respect of such termination payments. Taking into consideration whether the

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rating of the municipal obligor is below any applicable specified trigger, if the financial strength ratings of AGM were further downgraded below "A" by S&P or below "A2" by Moody's, and the conditions giving rise to the obligation of AGM to make a payment under the swap policies were all satisfied, then AGM could pay claims in an additional amount not exceeding approximately $455 million in respect of such termination payments.

As another example, with respect to variable rate demand obligations ("VRDOs") for which a bank has agreed to provide a liquidity facility, a downgrade of AGM or AGC may provide the bank with the right to give notice to bondholders that the bank will terminate the liquidity facility, causing the bondholders to tender their bonds to the bank. Bonds held by the bank accrue interest at a “bank bond rate” that is higher than the rate otherwise borne by the bond (typically the prime rate plus 2.00% — 3.00%, and capped at the lesser of 25% and the maximum legal limit). In the event the bank holds such bonds for longer than a specified period of time, usually 90-180 days, the bank has the right to demand accelerated repayment of bond principal, usually through payment of equal installments over a period of not less than five years. In the event that a municipal obligor is unable to pay interest accruing at the bank bond rate or to pay principal during the shortened amortization period, a claim could be submitted to AGM or AGC under its financial guaranty policy. As of June 30, 2016, AGM and AGC had insured approximately $5.4 billion net par of VRDOs, of which approximately $0.3 billion of net par constituted VRDOs issued by municipal obligors rated BBB- or lower pursuant to the Company’s internal rating. The specific terms relating to the rating levels that trigger the bank’s termination right, and whether it is triggered by a downgrade by one rating agency or a downgrade by all rating agencies then rating the insurer, vary depending on the transaction.

In addition, AGM may be required to pay claims in respect of AGMH’s former financial products business if Dexia SA and its affiliates, from which the Company had purchased AGMH and its subsidiaries, do not comply with their obligations following a downgrade of the financial strength rating of AGM. Most of the guaranteed investment contracts ("GICs") insured by AGM allow the GIC holder to terminate the GIC and withdraw the funds in the event of a downgrade of AGM below A3 or A-, with no right of the GIC issuer to avoid such withdrawal by posting collateral or otherwise enhancing its credit. Each GIC contract stipulates the thresholds below which the GIC issuer must post eligible collateral, along with the types of securities eligible for posting and the collateralization percentage applicable to each security type. These collateralization percentages range from 100% of the GIC balance for cash posted as collateral to, typically, 108% for asset-backed securities. If the entire aggregate accreted GIC balance of approximately $1.7 billion as of June 30, 2016 were terminated, the assets of the GIC issuers (which had an aggregate market value which exceed the liabilities by $0.8 billion) would be sufficient to fund the withdrawal of the GIC funds.

7. Fair Value Measurement

The Company carries a significant portion of its assets and liabilities at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e., exit price). The price represents the price available in the principal market for the asset or liability. If there is no principal market, then the price is based on a hypothetical market that maximizes the value received for an asset or minimizes the amount paid for a liability (i.e., the most advantageous market).

Fair value is based on quoted market prices, where available. If listed prices or quotes are not available, fair value is based on either internally developed models that primarily use, as inputs, market-based or independently sourced market parameters, including but not limited to yield curves, interest rates and debt prices or with the assistance of an independent third-party using a discounted cash flow approach and the third party’s proprietary pricing models. In addition to market information, models also incorporate transaction details, such as maturity of the instrument and contractual features designed to reduce the Company’s credit exposure, such as collateral rights as applicable.

Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments include amounts to reflect counterparty credit quality, the Company's creditworthiness and constraints on liquidity. As markets and products develop and the pricing for certain products becomes more or less transparent, the Company may refine its methodologies and assumptions. During Six Months 2016, no changes were made to the Company's valuation models that had or are expected to have, a material impact on the Company's consolidated balance sheets or statements of operations and comprehensive income.

The Company's methods for calculating fair value produce a fair value that may not be indicative of net realizable value or reflective of future fair values. The use of different methodologies or assumptions to determine fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The categorization within the fair value hierarchy is determined based on whether the inputs to valuation techniques used to measure fair value are observable or unobservable. Observable inputs reflect market data obtained from independent

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sources, while unobservable inputs reflect Company estimates of market assumptions. The fair value hierarchy prioritizes model inputs into three broad levels as follows, with Level 1 being the highest and Level 3 the lowest. An asset or liability's categorization is based on the lowest level of significant input to its valuation.

Level 1—Quoted prices for identical instruments in active markets. The Company generally defines an active market as a market in which trading occurs at significant volumes. Active markets generally are more liquid and have a lower bid-ask spread than an inactive market.

Level 2—Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and observable inputs other than quoted prices, such as interest rates or yield curves and other inputs derived from or corroborated by observable market inputs.

Level 3—Model derived valuations in which one or more significant inputs or significant value drivers are unobservable. Financial instruments are considered Level 3 when their values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation.

Transfers between Levels 1, 2 and 3 are recognized at the end of the period when the transfer occurs. The Company reviews the classification between Levels 1, 2 and 3 quarterly to determine whether a transfer is necessary. During the periods presented, there were no transfers between Level 1, 2 and 3.

Measured and Carried at Fair Value

Fixed-Maturity Securities and Short-Term Investments

The fair value of bonds in the investment portfolio is generally based on prices received from third party pricing services or alternative pricing sources with reasonable levels of price transparency. The pricing services prepare estimates of fair value measurements using their pricing models, which include available relevant market information, benchmark curves, benchmarking of like securities, and sector groupings. Additional valuation factors that can be taken into account are nominal spreads and liquidity adjustments. The pricing services evaluate each asset class based on relevant market and credit information, perceived market movements, and sector news. The market inputs used in the pricing evaluation include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data and industry and economic events. Benchmark yields have in many cases taken priority over reported trades for securities that trade less frequently or those that are distressed trades, and therefore may not be indicative of the market. The extent of the use of each input is dependent on the asset class and the market conditions. Given the asset class, the priority of the use of inputs may change or some market inputs may not be relevant. Additionally, the valuation of fixed-maturity investments is more subjective when markets are less liquid due to the lack of market based inputs, which may increase the potential that the estimated fair value of an investment is not reflective of the price at which an actual transaction would occur.

Short-term investments, that are traded in active markets, are classified within Level 1 in the fair value hierarchy and their value is based on quoted market prices. Securities such as discount notes are classified within Level 2 because these securities are typically not actively traded due to their approaching maturity and, as such, their cost approximates fair value. Short term securities that were obtained as part of loss mitigation efforts and whose prices were determined based on models, where at least one significant model assumption or input is unobservable, are considered to be Level 3 in the fair value hierarchy.

Annually, the Company reviews each pricing service's procedures, controls and models used in the valuations of the Company's investment portfolio, as well as the competency of the pricing service's key personnel. In addition, on a quarterly basis, the Company holds a meeting of the internal valuation committee (comprised of individuals within the Company with market, valuation, accounting, and/or finance experience) that reviews and approves prices and assumptions used by the pricing services.

For Level 1 and 2 securities, the Company, on a quarterly basis, reviews internally developed analytic packages that highlight, at a CUSIP level, price changes from the previous quarter to the current quarter. Where unexpected price movements are noted for a specific CUSIP, the Company formally challenges the price provided, and reviews all key inputs utilized in the third party's pricing model, and compares such information to management's own market information.

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For Level 3 securities, the Company, on a quarterly basis:

- reviews methodologies, any model updates and inputs and compares such information to management's own market information and, where applicable, the internal models,
- reviews internally developed analytic packages that highlight, at a CUSIP level, price changes from the previous quarter to the current quarter, and evaluates, documents, and resolves any significant pricing differences with the assistance of the third party pricing source, and
- compares prices received from different third party pricing sources, and evaluates, documents the rationale for, and resolves any significant pricing differences.

As of June 30, 2016, the Company used models to price 41 fixed-maturity securities (which were purchased or obtained for loss mitigation or other risk management purposes), which were 9.6% or $1,012 million of the Company's fixed-maturity securities and short-term investments at fair value. Most Level 3 securities were priced with the assistance of an independent third-party. The pricing is based on a discounted cash flow approach using the third-party's proprietary pricing models. The models use inputs such as projected prepayment speeds; severity assumptions; recovery lag assumptions; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); home price appreciation/depreciation rates based on macroeconomic forecasts and recent trading activity. The yield used to discount the projected cash flows is determined by reviewing various attributes of the bond including collateral type, weighted average life, sensitivity to losses, vintage, and convexity, in conjunction with market data on comparable securities. Significant changes to any of these inputs could materially change the expected timing of cash flows within these securities which is a significant factor in determining the fair value of the securities.

Other Invested Assets

As of June 30, 2016 and December 31, 2015, other invested assets include investments carried and measured at fair value on a recurring basis of $55 million and $53 million, respectively, and include primarily an investment in the global property catastrophe risk market and an investment in a fund that invests primarily in senior loans and bonds. Fair values for the majority of these investments are based on their respective net asset value ("NAV") per share or equivalent.

Other Assets

Committed Capital Securities

The fair value of committed capital securities ("CCS"), which is recorded in "other assets" on the consolidated balance sheets, represents the difference between the present value of remaining expected put option premium payments under AGC's CCS (the "AGC CCS") and AGM's Committed Preferred Trust Securities (the "AGM CPS") agreements, and the estimated present value that the Company would hypothetically have to pay currently for a comparable security (see Note 15, Long Term Debt and Credit Facilities). The AGC CCS and AGM CPS are carried at fair value with changes in fair value recorded in the consolidated statement of operations. The estimated current cost of the Company's CCS is based on several factors, including AGM and AGC CDS spreads, the U.S. dollar forward swap curve, London Interbank Offered Rate ("LIBOR") curve projections and the term the securities are estimated to remain outstanding.

Supplemental Executive Retirement Plans

The Company classifies the fair value measurement of the assets of the Company's various supplemental executive retirement plans as either Level 1 or Level 2. The fair value of these assets is valued based on the observable published daily values of the underlying mutual fund included in the aforementioned plans (Level 1) or based upon the NAV of the funds if a published daily value is not available (Level 2). The NAV are based on observable information.

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Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company’s credit derivatives consist primarily of insured CDS contracts, and also include interest rate swaps and hedges on other financial guarantors that fall under derivative accounting standards requiring fair value accounting through the statement of operations. The following is a description of the fair value methodology applied to the Company's insured credit default swaps that are accounted for as credit derivatives, which constitute the vast majority of the net credit derivative liability in the consolidated balance sheets. The Company did not enter into CDS with the intent to trade these contracts and the Company may not unilaterally terminate a CDS contract absent an event of default or termination event that entitles the Company to terminate such contracts; however, the Company has mutually agreed with various counterparties to terminate certain CDS transactions. Such terminations generally are not completed at fair value but instead for an amount that approximates the present value of future premiums or for a negotiated amount.

The terms of the Company’s CDS contracts differ from more standardized credit derivative contracts sold by companies outside the financial guaranty industry. The non-standard terms include the absence of collateral support agreements or immediate settlement provisions. In addition, the Company employs relatively high attachment points and does not exit derivatives it sells or purchases for credit protection purposes, except under specific circumstances such as mutual agreements with counterparties. Management considers the non-standard terms of its credit derivative contracts in determining the fair value of these contracts.

Due to the lack of quoted prices and other observable inputs for its instruments or for similar instruments, the Company determines the fair value of its credit derivative contracts primarily through internally developed, proprietary models that use both observable and unobservable market data inputs to derive an estimate of the fair value of the Company's contracts in its principal markets (see "Assumptions and Inputs"). There is no established market where financial guaranty insured credit derivatives are actively traded, therefore, management has determined that the exit market for the Company’s credit derivatives is a hypothetical one based on its entry market. Management has tracked the historical pricing of the Company’s deals to establish historical price points in the hypothetical market that are used in the fair value calculation. These contracts are classified as Level 3 in the fair value hierarchy since there is reliance on at least one unobservable input deemed significant to the valuation model, most importantly the Company’s estimate of the value of the non-standard terms and conditions of its credit derivative contracts and of the Company’s current credit standing.

The Company’s models and the related assumptions are continuously reevaluated by management and enhanced, as appropriate, based upon improvements in modeling techniques and availability of more timely and relevant market information.

The fair value of the Company’s credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay and the estimated present value of premiums that a financial guarantor of comparable credit-worthiness would hypothetically charge or pay at the reporting date for the same protection. The fair value of the Company’s credit derivatives depends on a number of factors, including notional amount of the contract, expected term, credit spreads, changes in interest rates, the credit ratings of referenced entities, the Company’s own credit risk and remaining contractual cash flows. The expected remaining contractual premium cash flows are the most readily observable inputs since they are based on the CDS contractual terms. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. Consistent with previous years, market conditions at June 30, 2016 were such that market prices of the Company’s CDS contracts were not available.

Management considers factors such as current prices charged for similar agreements, when available, performance of underlying assets, life of the instrument, and the nature and extent of activity in the financial guaranty credit derivative

marketplace. The assumptions that management uses to determine the fair value may change in the future due to market conditions. Due to the inherent uncertainties of the assumptions used in the valuation models, actual experience may differ from the estimates reflected in the Company's consolidated financial statements and the differences may be material.

Assumptions and Inputs

The various inputs and assumptions that are key to the establishment of the Company's fair value for CDS contracts are as follows:

•Gross spread.

•The allocation of gross spread among:
the profit the originator, usually an investment bank, realizes for putting the deal together and funding the transaction ("bank profit");

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premiums paid to the Company for the Company's credit protection provided ("net spread"); and
the cost of CDS protection purchased by the originator to hedge their counterparty credit risk exposure to the Company ("hedge cost").

- The weighted average life which is based on debt service schedules.

The rates used to discount future expected premium cash flows ranged from 0.47% to 1.72% at June 30, 2016 and 0.44% to 2.51% at December 31, 2015.

The Company obtains gross spreads on its outstanding contracts from market data sources published by third parties (e.g., dealer spread tables for the collateral similar to assets within the Company's transactions), as well as collateral-specific spreads provided by trustees or obtained from market sources. If observable market credit spreads are not available or reliable for the underlying reference obligations, then market indices are used that most closely resemble the underlying reference obligations, considering asset class, credit quality rating and maturity of the underlying reference obligations. These indices are adjusted to reflect the non-standard terms of the Company's CDS contracts. Market sources determine credit spreads by reviewing new issuance pricing for specific asset classes and receiving price quotes from their trading desks for the specific asset in question. Management validates these quotes by cross-referencing quotes received from one market source against quotes received from another market source to ensure reasonableness. In addition, the Company compares the relative change in price quotes received from one quarter to another, with the relative change experienced by published market indices for a specific asset class. Collateral specific spreads obtained from third-party, independent market sources are un-published spread quotes from market participants or market traders who are not trustees. Management obtains this information as the result of direct communication with these sources as part of the valuation process.

With respect to CDS transactions for which there is an expected claim payment within the next twelve months, the allocation of gross spread reflects a higher allocation to the cost of credit rather than the bank profit component. In the current market, it is assumed that a bank would be willing to accept a lower profit on distressed transactions in order to remove these transactions from its financial statements.

The following spread hierarchy is utilized in determining which source of gross spread to use, with the rule being to use CDS spreads where available. If not available, CDS spreads are either interpolated or extrapolated based on similar transactions or market indices.

- Actual collateral specific credit spreads (if up-to-date and reliable market-based spreads are available).
- Deals priced or closed during a specific quarter within a specific asset class and specific rating. No transactions closed during the periods presented.
- Credit spreads interpolated based upon market indices.
- Credit spreads provided by the counterparty of the CDS.
- Credit spreads extrapolated based upon transactions of similar asset classes, similar ratings, and similar time to maturity.

Information by Credit Spread Type (1)

	As of June 30, 2016		As of December 31, 2015	
Based on actual collateral specific spreads	13	%	13	%
Based on market indices	72	%	73	%
Provided by the CDS counterparty	15	%	14	%
Total	100	%	100	%

(1) Based on par.

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Over time the data inputs can change as new sources become available or existing sources are discontinued or are no longer considered to be the most appropriate. It is the Company's objective to move to higher levels on the hierarchy whenever possible, but it is sometimes necessary to move to lower priority inputs because of discontinued data sources or management's assessment that the higher priority inputs are no longer considered to be representative of market spreads for a given type of collateral. This can happen, for example, if transaction volume changes such that a previously used spread index is no longer viewed as being reflective of current market levels.

The Company interpolates a curve based on the historical relationship between the premium the Company receives when a credit derivative is closed to the daily closing price of the market index related to the specific asset class and rating of the deal. This curve indicates expected credit spreads at each indicative level on the related market index. For transactions with unique terms or characteristics where no price quotes are available, management extrapolates credit spreads based on a similar transaction for which the Company has received a spread quote from one of the first three sources within the Company's spread hierarchy. This alternative transaction will be within the same asset class, have similar underlying assets, similar credit ratings, and similar time to maturity. The Company then calculates the percentage of relative spread change quarter over quarter for the alternative transaction. This percentage change is then applied to the historical credit spread of the transaction for which no price quote was received in order to calculate the transactions' current spread. Counterparties determine credit spreads by reviewing new issuance pricing for specific asset classes and receiving price quotes from their trading desks for the specific asset in question. These quotes are validated by cross-referencing quotes received from one market source with those quotes received from another market source to ensure reasonableness.

The premium the Company receives is referred to as the "net spread." The Company's pricing model takes into account not only how credit spreads on risks that it assumes affect pricing, but also how the Company's own credit spread affects the pricing of its deals. The Company's own credit risk is factored into the determination of net spread based on the impact of changes in the quoted market price for credit protection bought on the Company, as reflected by quoted market prices on CDS referencing AGC or AGM. For credit spreads on the Company's name the Company obtains the quoted price of CDS contracts traded on AGC and AGM from market data sources published by third parties. The cost to acquire CDS protection referencing AGC or AGM affects the amount of spread on CDS deals that the Company retains and, hence, their fair value. As the cost to acquire CDS protection referencing AGC or AGM increases, the amount of premium the Company retains on a deal generally decreases. As the cost to acquire CDS protection referencing AGC or AGM decreases, the amount of premium the Company retains on a deal generally increases. In the Company's valuation model, the premium the Company captures is not permitted to go below the minimum rate that the Company would currently charge to assume similar risks. This assumption can have the effect of mitigating the amount of unrealized gains that are recognized on certain CDS contracts. Given the current market conditions and the Company's own credit spreads, approximately 16%, 18% and 20% based on number of deals, of the Company's CDS contracts are fair valued using this minimum premium as of June 30, 2016, March 31, 2016 and December 31, 2015, respectively. The percentage of deals that price using the minimum premiums fluctuates due to changes in AGM's and AGC's credit spreads. In general when AGM's and AGC's credit spreads narrow, the cost to hedge AGM's and AGC's name declines and more transactions price above previously established floor levels. Meanwhile, when AGM's and AGC's credit spreads widen, the cost to hedge AGM's and AGC's name increases causing more transactions to price at previously established floor levels. The Company corroborates the assumptions in its fair value model, including the portion of exposure to AGC and AGM hedged by its counterparties, with independent third parties each reporting period. The current level of AGC's and AGM's own credit spread has resulted in the bank or deal originator hedging a significant portion of its exposure to AGC and AGM. This reduces the amount of contractual cash flows AGC and AGM can capture as premium for selling its protection.

The amount of premium a financial guaranty insurance market participant can demand is inversely related to the cost of credit protection on the insurance company as measured by market credit spreads assuming all other assumptions remain constant. This is because the buyers of credit protection typically hedge a portion of their risk to the financial

guarantor, due to the fact that the contractual terms of the Company's contracts typically do not require the posting of collateral by the guarantor. The extent of the hedge depends on the types of instruments insured and the current market conditions.

A fair value resulting in a credit derivative asset on protection sold is the result of contractual cash inflows on in-force deals in excess of what a hypothetical financial guarantor could receive if it sold protection on the same risk as of the reporting date. If the Company were able to freely exchange these contracts (i.e., assuming its contracts did not contain proscriptions on transfer and there was a viable exchange market), it would be able to realize a gain representing the difference between the higher contractual premiums to which it is entitled and the current market premiums for a similar contract. The Company determines the fair value of its CDS contracts by applying the difference between the current net spread and the contractual net spread for the remaining duration of each contract to the notional value of its CDS contracts and taking the present value of such amounts discounted at the corresponding LIBOR over the weighted average remaining life of the contract.

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Example

The following is an example of how changes in gross spreads, the Company's own credit spread and the cost to buy protection on the Company affect the amount of premium the Company can demand for its credit protection. The assumptions used in these examples are hypothetical amounts. Scenario 1 represents the market conditions in effect on the transaction date and Scenario 2 represents market conditions at a subsequent reporting date.

	Scenario 1			Scenario 2		
	bps	% of Total		bps	% of Total	
Original gross spread/cash bond price (in bps)	185			500		
Bank profit (in bps)	115	62	%	50	10	%
Hedge cost (in bps)	30	16	%	440	88	%
The premium the Company receives per annum (in bps)	40	22	%	10	2	%

In Scenario 1, the gross spread is 185 basis points. The bank or deal originator captures 115 basis points of the original gross spread and hedges 10% of its exposure to AGC, when the CDS spread on AGC was 300 basis points (300 basis points × 10% = 30 basis points). Under this scenario the Company receives premium of 40 basis points, or 22% of the gross spread.

In Scenario 2, the gross spread is 500 basis points. The bank or deal originator captures 50 basis points of the original gross spread and hedges 25% of its exposure to AGC, when the CDS spread on AGC was 1,760 basis points (1,760 basis points × 25% = 440 basis points). Under this scenario the Company would receive premium of 10 basis points, or 2% of the gross spread. Due to the increased cost to hedge AGC's name, the amount of profit the bank would expect to receive, and the premium the Company would expect to receive decline significantly.

In this example, the contractual cash flows (the Company premium received per annum above) exceed the amount a market participant would require the Company to pay in today's market to accept its obligations under the CDS contract, thus resulting in an asset.

Strengths and Weaknesses of Model

The Company's credit derivative valuation model, like any financial model, has certain strengths and weaknesses.

The primary strengths of the Company's CDS modeling techniques are:

- The model takes into account the transaction structure and the key drivers of market value. The transaction structure includes par insured, weighted average life, level of subordination and composition of collateral.

- The model maximizes the use of market-driven inputs whenever they are available. The key inputs to the model are market-based spreads for the collateral, and the credit rating of referenced entities. These are viewed by the Company to be the key parameters that affect fair value of the transaction.

- The model is a consistent approach to valuing positions. The Company has developed a hierarchy for market-based spread inputs that helps mitigate the degree of subjectivity during periods of high illiquidity.

The primary weaknesses of the Company's CDS modeling techniques are:

- There is no exit market or actual exit transactions. Therefore the Company's exit market is a hypothetical one based on the Company's entry market.

- There is a very limited market in which to validate the reasonableness of the fair values developed by the Company's model.

- The markets for the inputs to the model were highly illiquid, which impacts their reliability.

- Due to the non-standard terms under which the Company enters into derivative contracts, the fair value of its credit derivatives may not reflect the same prices observed in an actively traded market of credit derivatives that do not contain terms and conditions similar to those observed in the financial guaranty market.

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These contracts were classified as Level 3 in the fair value hierarchy because there is a reliance on at least one unobservable input deemed significant to the valuation model, most significantly the Company's estimate of the value of non-standard terms and conditions of its credit derivative contracts and amount of protection purchased on AGC or AGM's name.

Fair Value Option on FG VIEs' Assets and Liabilities

The Company elected the fair value option for all the FG VIEs' assets and liabilities. See Note 9, Consolidated Variable Interest Entities.

The FG VIEs issued securities collateralized by first lien and second lien RMBS as well as loans and receivables. The lowest level input that is significant to the fair value measurement of these assets and liabilities was a Level 3 input (i.e., unobservable), therefore management classified them as Level 3 in the fair value hierarchy. Prices are generally determined with the assistance of an independent third-party, based on a discounted cash flow approach.

The models to price the FG VIEs' liabilities used, where appropriate, inputs such as estimated prepayment speeds; market values of the assets that collateralize the securities; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); yields implied by market prices for similar securities; house price depreciation/appreciation rates based on macroeconomic forecasts and, for those liabilities insured by the Company, the benefit from the Company's insurance policy guaranteeing the timely payment of principal and interest, taking into account the timing of the potential default and the Company's own credit rating. The third-party also utilizes an internal model to determine an appropriate yield at which to discount the cash flows of the security, by factoring in collateral types, weighted-average lives, and other structural attributes specific to the security being priced. The expected yield is further calibrated by utilizing algorithms designed to aggregate market color, received by the third-party, on comparable bonds.

The fair value of the Company's FG VIE assets is generally sensitive to changes related to estimated prepayment speeds; estimated default rates (determined on the basis of an analysis of collateral attributes such as: historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); discount rates implied by market prices for similar securities; and house price depreciation/appreciation rates based on macroeconomic forecasts. Significant changes to some of these inputs could materially change the market value of the FG VIE's assets and the implied collateral losses within the transaction. In general, the fair value of the FG VIE asset is most sensitive to changes in the projected collateral losses, where an increase in collateral losses typically leads to a decrease in the fair value of FG VIE assets, while a decrease in collateral losses typically leads to an increase in the fair value of FG VIE assets. These factors also directly impact the fair value of the Company's FG VIE liabilities.

The fair value of the Company's FG VIE liabilities is generally sensitive to the various model inputs described above. In addition, the Company's FG VIE liabilities with recourse are also sensitive to changes in the Company's implied credit worthiness. Significant changes to any of these inputs could materially change the timing of expected losses within the insured transaction which is a significant factor in determining the implied benefit from the Company's insurance policy guaranteeing the timely payment of principal and interest for the tranches of debt issued by the FG VIE that is insured by the Company. In general, extending the timing of expected loss payments by the Company into the future typically leads to a decrease in the value of the Company's insurance and a decrease in the fair value of the Company's FG VIE liabilities with recourse, while a shortening of the timing of expected loss payments by the Company typically leads to an increase in the value of the Company's insurance and an increase in the fair value of the Company's FG VIE liabilities with recourse.

Not Carried at Fair Value

Financial Guaranty Insurance Contracts

For financial guaranty insurance contracts that are acquired in a business combination, the Company measures each contract at fair value on the date of acquisition, and then follows insurance accounting guidance on a recurring basis thereafter. On a quarterly basis, the Company also discloses the fair value of its outstanding financial guaranty insurance contracts. In both cases, fair value is based on management's estimate of what a similarly rated financial guaranty insurance company would demand to acquire the Company's in-force book of financial guaranty insurance business. It is based on a variety of factors that may include pricing assumptions management has observed for portfolio transfers, commutations, and acquisitions that have occurred in the financial guaranty market, as well as prices observed in the credit derivative market with an adjustment for illiquidity so that the terms would be similar to a financial guaranty insurance contract, and includes adjustments to the carrying value of unearned premium reserve for stressed losses, ceding commissions and return on capital. The significant inputs were not readily observable. The Company accordingly classified this fair value measurement as Level 3.

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Long-Term Debt

The Company's long-term debt, excluding notes payable, is valued by broker-dealers using third party independent pricing sources and standard market conventions. The market conventions utilize market quotations, market transactions for the Company's comparable instruments, and to a lesser extent, similar instruments in the broader insurance industry. The fair value measurement was classified as Level 2 in the fair value hierarchy.

The fair value of the notes payable was determined by calculating the present value of the expected cash flows. The Company determines discounted future cash flows using market driven discount rates and a variety of assumptions, including a projection of the LIBOR rate, prepayment and default assumptions, and AGM CDS spreads. The fair value measurement was classified as Level 3 in the fair value hierarchy because there is a reliance on significant unobservable inputs to the valuation model, including the discount rates, prepayment and default assumptions, loss severity and recovery on delinquent loans.

Other Invested Assets

The other invested assets not carried at fair value consist primarily of investments in a guaranteed investment contract for future claims payments. The fair value of the investments in the guaranteed investment contract approximated their carrying value due to their short term nature. The fair value measurement of the investments in the guaranteed investment contract was classified as Level 2 in the fair value hierarchy.

Other Assets and Other Liabilities

The Company's other assets and other liabilities consist predominantly of accrued interest, receivables for securities sold and payables for securities purchased, the carrying values of which approximate fair value.

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Financial Instruments Carried at Fair Value

Amounts recorded at fair value in the Company's financial statements are presented in the tables below.

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of June 30, 2016

		Fair Value Hierarchy		
	Fair Value	Level 1	Level 2	Level 3
	(in millions)			
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$5,603	$—	$5,562	$41
U.S. government and agencies	326	—	326	—
Corporate securities	1,443	—	1,385	58
Mortgage-backed securities:				
RMBS	1,062	—	713	349
Commercial mortgage-backed securities ("CMBS")	539	—	539	—
Asset-backed securities	730	—	166	564
Foreign government securities	257	—	257	—
Total fixed-maturity securities	9,960	—	8,948	1,012
Short-term investments	585	521	64	—
Other invested assets (1)	13	—	6	7
Credit derivative assets	36	—	—	36
FG VIEs' assets, at fair value	814	—	—	814
Other assets	84	22	27	35
Total assets carried at fair value	$11,492	$543	$9,045	$1,904
Liabilities:				
Credit derivative liabilities	$432	$—	$—	$432
FG VIEs' liabilities with recourse, at fair value	790	—	—	790
FG VIEs' liabilities without recourse, at fair value	115	—	—	115
Total liabilities carried at fair value	$1,337	$—	$—	$1,337

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Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2015

		Fair Value Hierarchy		
	Fair Value	Level 1	Level 2	Level 3
	(in millions)			
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities				
Obligations of state and political subdivisions	$5,841	$—	$5,833	$8
U.S. government and agencies	400	—	400	—
Corporate securities	1,520	—	1,449	71
Mortgage-backed securities:				
RMBS	1,245	—	897	348
CMBS	513	—	513	—
Asset-backed securities	825	—	168	657
Foreign government securities	283	—	283	—
Total fixed-maturity securities	10,627	—	9,543	1,084
Short-term investments	396	305	31	60
Other invested assets (1)	12	—	5	7
Credit derivative assets	81	—	—	81
FG VIEs' assets, at fair value	1,261	—	—	1,261
Other assets	106	23	21	62
Total assets carried at fair value	$12,483	$328	$9,600	$2,555
Liabilities:				
Credit derivative liabilities	$446	$—	$—	$446
FG VIEs' liabilities with recourse, at fair value	1,225	—	—	1,225
FG VIEs' liabilities without recourse, at fair value	124	—	—	124
Total liabilities carried at fair value	$1,795	$—	$—	$1,795

(1) Excluded from the table above are investments funds of $46 million and $45 million as of June 30, 2016 and December 31, 2015, respectively, measured using NAV per share. Includes Level 3 mortgage loans that are recorded at fair value on a non-recurring basis.

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Changes in Level 3 Fair Value Measurements

The table below presents a roll forward of the Company's Level 3 financial instruments carried at fair value on a recurring basis during Second Quarter 2016 and 2015 and Six Months 2016 and 2015.

Fair Value Level 3 Rollforward
Recurring Basis
Second Quarter 2016

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Short-Term Investments	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)									
Fair value as of March 31, 2016	$7	$74	$360	$639	$—	$1,191	$49	$(434)	$(1,165)	$(119)
Total pretax realized and unrealized gains/(losses) recorded in: (1)										
Net income (loss)	0 (2)	2 (2)	4 (2)	10 (2)	—	113 (3)	(11) (4)	63 (6)	(112) (3)	2 (3)
Other comprehensive income (loss)	1	(18)	3	(5)	—	—	0	—	—	—
Purchases	33	—	6	—	—	—	—	—	—	—
Settlements	—	—	(24)	(80)	—	(490)	—	(25)	487	2
FG VIE consolidations	—	—	—	—	—	—	—	—	—	—
FG VIE deconsolidations	—	—	—	—	—	—	—	—	—	—
Fair value as of June 30, 2016	$41	$58	$349	$564	$—	$814	$38	$(396)	$(790)	$(115)
Change in unrealized gains/(losses) related to financial instruments held as of June 30, 2016	$1	$(18)	$2	$(4)	$—	$11	$(11)	$(20)	$(2)	$2

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Fair Value Level 3 Rollforward
Recurring Basis
Second Quarter 2015

	Fixed-Maturity Securities								
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)								
Fair value as of March 31, 2015	$8	$ 79	$383	$ 226	$1,495	$40	$ (782)	$ (1,278)	$ (145)
Radian Asset Acquisition	—	—	4	—	122	2	(215)	(114)	(4)
Total pretax realized and unrealized gains/(losses) recorded in: (1)									
Net income (loss)	0 (2)	(3) (2)	8 (2)	3 (2)	19 (3)	23 (4)	90 (6)	(5) (3)	(25) (3)
Other comprehensive income (loss)	(1)	1	(9)	8	—	(1)	—	—	—
Purchases	—	—	1	—	—	—	—	—	—
Settlements	— (7)	—	(51)	(1)	(40)	—	(19)	36	3
FG VIE consolidations	—	—	(1)	—	—	—	—	—	—
FG VIE deconsolidations	—	—	—	—	—	—	—	—	—
Fair value as of June 30, 2015	$7	$ 77	$335	$ 236	$1,596	$64	$ (926)	$ (1,361)	$ (171)
Change in unrealized gains/(losses) related to financial instruments held as of June 30, 2015	$0	$ 1	$(7)	$ 8	$31	$22	$ 82	$ (6)	$ (14)

Fair Value Level 3 Rollforward
Recurring Basis
Six Months 2016

	Fixed-Maturity Securities									
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	Short-Term Investments	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse,	FG VIEs' Liabilities without Recourse, at Fair

									at Fair Value	Value
	(in millions)									
Fair value as of December 31, 2015	$8	$71	$348	$657	$60	$1,261	$65	$(365)	$(1,225)	$(124)
Total pretax realized and unrealized gains/(losses) recorded in: (1)										
Net income (loss)	0	(2) 4	(2) 2	(2) 11	(2) 0	(2) 109	(3) (27)	(4) 3	(6) (91)	(3) 4 (3)
Other comprehensive income (loss)	1	(17)	(2)	(10)	0	—	0	—	—	—
Purchases	33	—	40	—	—	—	—	—	—	—
Settlements	(1)	—	(39)	(94)	(60)	(556)	—	(34)	526	5
FG VIE consolidations	—	—	—	—	—	—	—	—	—	—
FG VIE deconsolidations	—	—	0	—	—	0	—	—	0	—
Fair value as of June 30, 2016	$41	$58	$349	$564	$—	$814	$38	$(396)	$(790)	$(115)
Change in unrealized gains/(losses) related to financial instruments held as of June 30, 2016	$1	$(17)	$(3)	$(10)	$—	$15	$(27)	$(99)	$19	$3

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Fair Value Level 3 Rollforward
Recurring Basis
Six Months 2015

	Fixed-Maturity Securities								
	Obligations of State and Political Subdivisions	Corporate Securities	RMBS	Asset-Backed Securities	FG VIEs' Assets at Fair Value	Other Assets (8)	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)								
Fair value as of December 31, 2014	$38	$ 79	$425	$ 228	$1,398	$ 37	$ (895)	$ (1,277)	$ (142)
Radian Asset Acquisition	—	—	4	—	122	2	(215)	(114)	(4)
Total pretax realized and unrealized gains/(losses) recorded in: (1)									
Net income (loss)	3 (2)	(1) (2)	17 (2)	1 (2)	42 (3)	25 (4)	214 (6)	88 (3)	(30) (3)
Other comprehensive income (loss)	(3)	(1)	(4)	9	—	—	—	—	—
Purchases	—	—	10	—	—	—	—	—	—
Settlements	(31)	(7) —	(116)	(2)	(70)	0	(30)	73	5
FG VIE consolidations	—	—	(1)	—	104	—	—	(131)	—
FG VIE deconsolidations	—	—	—	—	—	—	—	—	—
Fair value as of June 30, 2015	$7	$ 77	$335	$ 236	$1,596	$ 64	$ (926)	$ (1,361)	$ (171)
Change in unrealized gains/(losses) related to financial instruments held as of June 30, 2015	$0	$ (1)	$(1)	$ 9	$65	$ 25	$ 186	$ (12)	$ (19)

(1) Realized and unrealized gains (losses) from changes in values of Level 3 financial instruments represent gains (losses) from changes in values of those financial instruments only for the periods in which the instruments were classified as Level 3.

(2) Included in net realized investment gains (losses) and net investment income.

(3) Included in fair value gains (losses) on FG VIEs.

(4) Recorded in fair value gains (losses) on CCS, net investment income and other income.

(5) Represents net position of credit derivatives. The consolidated balance sheet presents gross assets and liabilities based on net counterparty exposure.

(6) Reported in net change in fair value of credit derivatives.

(7) Primarily non-cash transaction.

(8) Includes CCS and other invested assets.

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Level 3 Fair Value Disclosures

Quantitative Information About Level 3 Fair Value Inputs
At June 30, 2016

Financial Instrument Description (1)	Fair Value at June 30, 2016 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets (2):				
Fixed-maturity securities:				
Obligations of state and political subdivisions	$ 41	Yield	4.3 %-18.4%	13.2%
Corporate securities	58	Yield	20.3%	
RMBS	349	CPR	1.6 %-9.5%	3.3%
		CDR	0.1 %-12.4%	9.4%
		Loss severity	50.0 %-100.0%	75.2%
		Yield	4.8 %-8.5%	6.0%
Asset-backed securities:				
Triple-X life insurance transactions	321	Yield	4.3 %-6.8%	5.1%
Collateralized debt obligations ("CDO")	243	Yield	15.0%	
FG VIEs' assets, at fair value	814	CPR	2.5 %-8.0%	5.1%
		CDR	1.2 %-16.3%	5.8%
		Loss severity	50.0 %-100.0%	85.4%
		Yield	3.2 %-21.5%	7.0%
Other assets	35	Estimated pricing	$59 -$61	$60
		Term (years)	5 years	
Liabilities:				
Credit derivative liabilities, net	(396)	Year 1 loss estimates	0.0 %-37.0%	0.9%
		Hedge cost (in bps)	11.3 -198.8	39.1
		Bank profit (in bps)	3.8 -1,572.5	99.7
		Internal floor (in bps)	7.0 -100.0	27.9
		Internal credit rating	AAA -CCC	AA
FG VIEs' liabilities, at fair value	(905)	CPR	2.5 %-8.0%	5.1%
		CDR	1.2 %-16.3%	5.8%
		Loss severity	50.0 %-100.0%	85.4%
		Yield	3.2 %-21.5%	5.8%

(1) Discounted cash flow is used as valuation technique for all financial instruments.

(2) Excludes several investments recorded in other invested assets with fair value of $7 million.

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Quantitative Information About Level 3 Fair Value Inputs
At December 31, 2015

Financial Instrument Description (1)	Fair Value at December 31, 2015 (in millions)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
Assets (2):				
Fixed-maturity securities (3):				
Corporate securities	$ 71	Yield	21.8%	
RMBS	348	CPR	0.3 %-9.0%	2.6%
		CDR	2.7 %-9.3%	7.0%
		Loss severity	60.0 %-100.0%	74.0%
		Yield	4.7 %-8.2%	6.0%
Asset-backed securities:				
Investor owned utility	69	Cash flow receipts	100.0%	
		Collateral recovery period	2.9 years	
		Discount factor	7.0%	
Triple-X life insurance transactions	329	Yield	3.5 %-7.5%	5.0%
CDO	259	Yield	20.0%	
Short-term investments	60	Yield	17.0%	
FG VIEs' assets, at fair value	1,261	CPR	0.3 %-9.2%	3.9%
		CDR	1.2 %-16.0%	4.7%
		Loss severity	40.0 %-100.0%	85.9%
		Yield	1.9 %-20.0%	6.4%
Other assets	62	Quotes from third party pricing	$44 -$46	$45
		Term (years)	5 years	
Liabilities:				
Credit derivative liabilities, net	(365)	Year 1 loss estimates	0.0 %-41.0%	0.6%
		Hedge cost (in bps)	32.8 -282.0	66.3
		Bank profit (in bps)	3.8 -1,017.5	110.8
		Internal floor (in bps)	7.0 -100.0	16.8
		Internal credit rating	AAA -CCC	AA+
FG VIEs' liabilities, at fair value	(1,349)	CPR	0.3 %-9.2%	3.9%
		CDR	1.2 %-16.0%	4.7%
		Loss severity	40.0 %-100.0%	85.9%
		Yield	1.9 %-20.0%	5.6%

(1) Discounted cash flow is used as valuation technique for all financial instruments.

(2) Excludes several investments recorded in other invested assets with fair value of $7 million.

(3) Excludes obligations of state and political subdivisions investments with fair value of $8 million.

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The carrying amount and estimated fair value of the Company's financial instruments are presented in the following table.

Fair Value of Financial Instruments

	As of June 30, 2016		As of December 31, 2015	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in millions)			
Assets:				
Fixed-maturity securities	$9,960	$ 9,960	$10,627	$ 10,627
Short-term investments	585	585	396	396
Other invested assets (1)	155	157	150	152
Credit derivative assets	36	36	81	81
FG VIEs' assets, at fair value	814	814	1,261	1,261
Other assets	187	187	206	206
Liabilities:				
Financial guaranty insurance contracts (2)	3,690	9,928	3,998	8,712
Long-term debt	1,303	1,527	1,300	1,512
Credit derivative liabilities	432	432	446	446
FG VIEs' liabilities with recourse, at fair value	790	790	1,225	1,225
FG VIEs' liabilities without recourse, at fair value	115	115	124	124
Other liabilities	7	7	9	9

(1) Includes investments not carried at fair value with a carrying value of $96 million and $93 million as of June 30, 2016 and December 31, 2015, respectively. Excludes investments carried under the equity method.

(2) Carrying amount includes the assets and liabilities related to financial guaranty insurance contract premiums, losses, and salvage and subrogation and other recoverables net of reinsurance.

8. Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company has a portfolio of financial guaranty contracts that meet the definition of a derivative in accordance with GAAP (primarily CDS).

Credit derivative transactions are governed by ISDA documentation and have different characteristics from financial guaranty insurance contracts. For example, the Company's control rights with respect to a reference obligation under a credit derivative may be more limited than when the Company issues a financial guaranty insurance contract. In addition, there are more circumstances under which the Company may be obligated to make payments. Similar to a financial guaranty insurance contract, the Company would be obligated to pay if the obligor failed to make a scheduled payment of principal or interest in full. However, the Company may also be required to pay if the obligor becomes bankrupt or if the reference obligation were restructured if, after negotiation, those credit events are specified in the documentation for the credit derivative transactions. Furthermore, the Company may be required to make a payment due to an event that is unrelated to the performance of the obligation referenced in the credit derivative. If events of default or termination events specified in the credit derivative documentation were to occur, the non-defaulting or the non-affected party, which may be either the Company or the counterparty, depending upon the circumstances, may decide to terminate a credit derivative prior to maturity. In that case, the Company may be

required to make a termination payment to its swap counterparty upon such termination. Absent such an event of default or termination event, the Company may not unilaterally terminate a CDS contract; however, the Company on occasion has mutually agreed with various counterparties to terminate certain CDS transactions.

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Credit Derivative Net Par Outstanding by Sector

The estimated remaining weighted average life of credit derivatives was 5.0 years at June 30, 2016 and 5.4 years at December 31, 2015. The components of the Company's credit derivative net par outstanding are presented below.

Credit Derivatives
Subordination and Ratings

Asset Type	As of June 30, 2016				As of December 31, 2015			
	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating	Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating
	(dollars in millions)							
Pooled corporate obligations:								
Collateralized loan obligation/collateral bond obligations	$3,006	29.7 %	55.8 %	AAA	$5,873	30.9 %	42.3 %	AAA
Synthetic investment grade pooled corporate	7,116	21.7	19.4	AAA	7,108	21.7	19.4	AAA
TruPS CDOs	2,531	45.3	44.0	A-	3,429	45.8	42.6	A-
Market value CDOs of corporate obligations	—	—	—	--	1,113	17.0	30.1	AAA
Total pooled corporate obligations	12,653	28.3	33.0	AAA	17,523	29.2	32.3	AAA
U.S. RMBS:								
Option ARM and Alt-A first lien	289	9.5	13.1	AA-	351	10.5	12.7	AA-
Subprime first lien	925	27.7	45.3	AA	981	27.7	45.2	AA
Prime first lien	—	—	—	--	177	10.9	0.0	BB
Closed-end second lien	15	—	—	CCC	17	—	—	CCC
Total U.S. RMBS	1,229	25.1	40.7	AA	1,526	24.1	37.4	A+
CMBS	384	44.8	58.4	AAA	530	44.8	52.6	AAA
Other	5,748	—	—	A	6,015	—	—	A
Total	$20,014			AA	$25,594			AA+

(1) Represents the sum of subordinate tranches and over-collateralization and does not include any benefit from excess interest collections that may be used to absorb losses.

Except for TruPS CDOs, the Company's exposure to pooled corporate obligations is highly diversified in terms of obligors and industries. Most pooled corporate transactions are structured to limit exposure to any given obligor and industry. The majority of the Company's pooled corporate exposure consists of collateralized loan obligation ("CLO") or synthetic pooled corporate obligations. Most of these CLOs have an average obligor size of less than 1% of the total transaction and typically restrict the maximum exposure to any one industry to approximately 10%. The Company's exposure also benefits from embedded credit enhancement in the transactions which allows a transaction to sustain a certain level of losses in the underlying collateral, further insulating the Company from industry specific concentrations of credit risk on these deals.

The Company's TruPS CDO asset pools are generally less diversified by obligors and industries than the typical CLO asset pool. Also, the underlying collateral in TruPS CDOs consists primarily of subordinated debt instruments such as

TruPS issued by bank holding companies and similar instruments issued by insurance companies, real estate investment trusts and other real estate related issuers while CLOs typically contain primarily senior secured obligations. However, to mitigate these risks TruPS CDOs were typically structured with higher levels of embedded credit enhancement than typical CLOs.

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The Company's exposure to "Other" CDS contracts is also highly diversified. It includes $1.6 billion of exposure to one pooled infrastructure transaction comprising diversified pools of international infrastructure project transactions and loans to regulated utilities. These pools were all structured with underlying credit enhancement sufficient for the Company to attach at AAA levels at origination. The remaining $4.1 billion of exposure in "Other" CDS contracts comprises numerous deals across various asset classes, such as commercial receivables, international RMBS, infrastructure, regulated utilities and consumer receivables.

Distribution of Credit Derivative Net Par Outstanding by Internal Rating

	As of June 30, 2016		As of December 31, 2015	
Ratings	Net Par Outstanding	% of Total	Net Par Outstanding	% of Total
	(dollars in millions)			
AAA	$10,966	54.8 %	$14,808	57.9 %
AA	4,137	20.7	4,821	18.8
A	2,067	10.3	2,144	8.4
BBB	1,758	8.8	2,212	8.6
BIG	1,086	5.4	1,609	6.3
Credit derivative net par outstanding	$20,014	100.0 %	$25,594	100.0 %

Fair Value of Credit Derivatives

Net Change in Fair Value of Credit Derivatives Gain (Loss)

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Realized gains on credit derivatives	$18	$15	$28	$38
Net credit derivative losses (paid and payable) recovered and recoverable and other settlements	6	(7)	4	(9)
Realized gains (losses) and other settlements	24	8	32	29
Net unrealized gains (losses):				
Pooled corporate obligations	8	7	(40)	24
U.S. RMBS	27	62	12	137
CMBS	0	4	0	4
Other	4	9	(1)	20
Net unrealized gains (losses)	39	82	(29)	185
Net change in fair value of credit derivatives	$63	$90	$3	$214

Net Par and Realized Gains
from Terminations and Settlements of Credit Derivative Contracts

	Second Quarter		Six Months	
	2016	2015	2016	2015

	(in millions)			
Net par of terminated credit derivative contracts	$2,436	$471	$2,436	$564
Realized gains on credit derivatives	8	2	8	13
Net unrealized gains (losses) on credit derivatives	59	0	70	(1)

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During Second Quarter 2016, unrealized fair value gains were generated primarily as a result of CDS terminations. The Company reached a settlement agreement with two CDS counterparties to terminate several CDS transactions. This was the primary driver of the unrealized fair value gains in the U.S. RMBS, pooled corporate CLO, and Other sectors. The unrealized fair value gains were partially offset by unrealized losses resulting from wider implied net spreads across all sectors. The wider implied net spreads were primarily a result of the decreased cost to buy protection in AGC's and AGM's name, particularly for the one year CDS spread, as the market cost of AGC's and AGM's credit protection decreased significantly during the period. For those CDS transactions that were pricing at or above their floor levels, when the cost of purchasing CDS protection on AGC and AGM decreased, the implied spreads that the Company would expect to receive on these transactions increased.

During Six Months 2016, unrealized fair value losses were generated primarily in the TruPS CDO sector, due to wider implied net spreads. The wider implied net spreads were primarily a result of the decreased cost to buy protection in AGC's and AGM's name, particularly for the one year and five year CDS spread, as the market cost of AGC's and AGM's credit protection decreased during the period. For those CDS transactions that were pricing at or above their floor levels, when the cost of purchasing CDS protection on AGC and AGM decreased, the implied spreads that the Company would expect to receive on these transactions increased. The unrealized fair value losses were partially offset by unrealized fair value gains which resulted from the terminations of several CDS transactions during the period. The majority of the CDS transactions were terminated as a result of settlement agreements with two CDS counterparties in Second Quarter 2016, as discussed above.

During Second Quarter 2015, unrealized fair value gains were generated primarily in the TruPS CDO sector, and U.S. RMBS prime first lien and Option ARM and subprime sectors, due to tighter implied net spreads. The tighter implied net spreads were primarily a result of the increased cost to buy protection in AGC's and AGM's name, particularly for the one year and five year CDS spread, as the market cost of AGC's and AGM's credit protection increased during the period. For those CDS transactions that were pricing above their floor levels, when the cost of purchasing CDS protection on AGC and AGM increased, the implied spreads that the Company would expect to receive on these transactions decreased.

During Six Months 2015, unrealized fair value gains were generated primarily in the TruPS CDO sector, and U.S. RMBS prime first lien and Option ARM and subprime sectors, due to tighter implied net spreads. The tighter implied net spreads were primarily a result of the increased cost to buy protection in AGC's and AGM's name, particularly for the one year and five year CDS spread, as the market cost of AGC's and AGM's credit protection increased during the period. For those CDS transactions that were pricing above their floor levels, when the cost of purchasing CDS protection on AGC and AGM increased, the implied spreads that the Company would expect to receive on these transactions decreased. In addition, during Six Months 2015 there was a refinement in methodology to address an instance in a U.S. RMBS transaction that changed from an expected loss to an expected recovery position. This refinement resulted in approximately $49 million in fair value gains in Six Months 2015.

The impact of changes in credit spreads will vary based upon the volume, tenor, interest rates, and other market conditions at the time these fair values are determined. In addition, since each transaction has unique collateral and structural terms, the underlying change in fair value of each transaction may vary considerably. The fair value of credit derivative contracts also reflects the change in the Company's own credit cost based on the price to purchase credit protection on AGC and AGM. The Company determines its own credit risk based on quoted CDS prices traded on the Company at each balance sheet date.

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CDS Spread on AGC and AGM
Quoted price of CDS contract (in basis points)

	As of June 30, 2016	As of March 31, 2016	As of December 31, 2015	As of June 30, 2015	As of March 31, 2015	As of December 31, 2014
Five-year CDS spread:						
AGC	265	307	376	390	317	323
AGM	265	309	366	410	341	325
One-year CDS spread						
AGC	45	105	139	120	60	80
AGM	47	102	131	125	80	85

Fair Value of Credit Derivatives Assets (Liabilities)
and Effect of AGC and AGM
Credit Spreads

	As of June 30, 2016	As of December 31, 2015
	(in millions)	
Fair value of credit derivatives before effect of AGC and AGM credit spreads	$(1,170)	$ (1,448)
Plus: Effect of AGC and AGM credit spreads	774	1,083
Net fair value of credit derivatives	$(396)	$ (365)

The fair value of CDS contracts at June 30, 2016, before considering the implications of AGC's and AGM's credit spreads, is a direct result of continued wide credit spreads in the fixed income security markets and ratings downgrades. The asset classes that remain most affected are TruPS and pooled corporate securities as well as 2005-2007 vintages of prime first lien, Alt-A, Option ARM and subprime RMBS deals. Comparing June 30, 2016 with December 31, 2015, there were several CDS terminations as well as a narrowing of spreads primarily related to the Company's TruPS obligations which resulted in mark to market benefit.

Management believes that the trading level of AGC's and AGM's credit spreads over the past several years has been due to the correlation between AGC's and AGM's risk profile and the current risk profile of the broader financial markets, as well as the overall lack of liquidity in the CDS market. Offsetting the benefit attributable to AGC's and AGM's credit spread were higher credit spreads in the fixed income security markets. The higher credit spreads in the fixed income security market are due to the lack of liquidity in the high yield CDO, TruPS CDO, and CLO markets as well as continuing market concerns over the 2005-2007 vintages of RMBS.

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The following table presents the fair value and the present value of expected claim payments or recoveries (i.e. net expected loss to be paid as described in Note 5) for contracts accounted for as derivatives.

Net Fair Value and Expected Losses
of Credit Derivatives by Sector

	Fair Value of Credit Derivative Asset (Liability), net		Expected Loss to be (Paid) Recovered	
Asset Type	As of June 30, 2016	As of December 31, 2015	As of June 30, 2016	As of December 31, 2015
	(in millions)			
Pooled corporate obligations	$ (124)	$ (82)	$ (4)	$ (5)
U.S. RMBS	(86)	(98)	(29)	(38)
Other	(186)	(185)	29	27
Total	$ (396)	$ (365)	$ (4)	$ (16)

Ratings Sensitivities of Credit Derivative Contracts

Within the Company's insured CDS portfolio, the transaction documentation for approximately $1.0 billion in CDS gross par insured as of June 30, 2016 requires AGC to post eligible collateral to secure its obligations to make payments under such contracts. This constitutes a $2.7 billion reduction from the $3.7 billion in CDS gross par insured subject to such a requirement as of March 31, 2016, primarily due to an agreement reached in May 2016 with a CDS counterparty reducing the collateral posting requirement with that counterparty to zero. Eligible collateral is generally cash or U.S. government or agency securities; eligible collateral other than cash is valued at a discount to the face amount.

- For approximately $0.8 billion of such contracts, AGC has negotiated caps such that the posting requirement cannot exceed a certain fixed amount, regardless of the mark-to-market valuation of the exposure or the financial strength ratings of AGC. For such contracts, AGC need not post on a cash basis an aggregate of more than $500 million, although the value of the collateral posted may exceed such fixed amount depending on the advance rate agreed with the counterparty for the particular type of collateral posted. The May 2016 agreement with the CDS counterparty mentioned above had the effect of reducing the aggregate cap on the amount AGC would be required to post on a cash basis from $575 million as of March 31, 2016, to $500 million as of June 30, 2016.

- For the remaining approximately $208 million of such contracts, AGC could be required from time to time to post additional collateral without such cap based on movements in the mark-to-market valuation of the underlying exposure.

As of June 30, 2016, the Company was posting approximately $216 million to secure its obligations under CDS, of which approximately $17 million related to the $208 million of notional described above, as to which the obligation to collateralize is not capped. As of December 31, 2015, the Company was posting approximately $305 million to secure its obligations under CDS, of which approximately $23 million related to $221 million of notional as to which the obligation to collateralize was not capped. The obligation to post collateral could impair the Company's liquidity and results of operations.

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Sensitivity to Changes in Credit Spread

The following table summarizes the estimated change in fair values on the net balance of the Company's credit derivative positions assuming immediate parallel shifts in credit spreads on AGC and AGM and on the risks that they both assume.

Effect of Changes in Credit Spread
As of June 30, 2016

Credit Spreads(1)	Estimated Net Fair Value (Pre-Tax)	Estimated Change in Gain/(Loss) (Pre-Tax)
	(in millions)	
100% widening in spreads	$(805)	$ (409)
50% widening in spreads	(601)	(205)
25% widening in spreads	(499)	(103)
10% widening in spreads	(437)	(41)
Base Scenario	(396)	—
10% narrowing in spreads	(358)	38
25% narrowing in spreads	(301)	95
50% narrowing in spreads	(206)	190

(1) Includes the effects of spreads on both the underlying asset classes and the Company's own credit spread.

9. Consolidated Variable Interest Entities

Consolidated FG VIEs

The Company provides financial guaranties with respect to debt obligations of special purpose entities, including VIEs. Assured Guaranty does not act as the servicer or collateral manager for any VIE obligations insured by its companies. The transaction structure generally provides certain financial protections to the Company. This financial protection can take several forms, the most common of which are overcollateralization, first loss protection (or subordination) and excess spread. In the case of overcollateralization (i.e., the principal amount of the securitized assets exceeds the principal amount of the structured finance obligations guaranteed by the Company), the structure allows defaults of the securitized assets before a default is experienced on the structured finance obligation guaranteed by the Company. In the case of first loss, the financial guaranty insurance policy only covers a senior layer of losses experienced by multiple obligations issued by special purpose entities, including VIEs. The first loss exposure with respect to the assets is either retained by the seller or sold off in the form of equity or mezzanine debt to other investors. In the case of excess spread, the financial assets contributed to special purpose entities, including VIEs, generate interest income that are in excess of the interest payments on the debt issued by the special purpose entity. Such excess spread is typically distributed through the transaction's cash flow waterfall and may be used to create additional credit enhancement, applied to redeem debt issued by the special purpose entities, including VIEs (thereby, creating additional overcollateralization), or distributed to equity or other investors in the transaction.

Assured Guaranty is not primarily liable for the debt obligations issued by the VIEs it insures and would only be required to make payments on those insured debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due and only for the amount of the shortfall. AGL's and its Subsidiaries' creditors do not have any rights with regard to the collateral supporting the debt issued by the FG VIEs. Proceeds from sales,

maturities, prepayments and interest from such underlying collateral may only be used to pay debt service on VIE liabilities. Net fair value gains and losses on FG VIEs are expected to reverse to zero at maturity of the VIE debt, except for net premiums received and net claims paid by Assured Guaranty under the financial guaranty insurance contract. The Company’s estimate of expected loss to be paid for FG VIEs is included in Note 5, Expected Loss to be Paid.

As part of the terms of its financial guaranty contracts, the Company obtains certain protective rights with respect to the VIE that are triggered by the occurrence of certain events, such as failure to be in compliance with a covenant due to poor deal performance or a deterioration in a servicer or collateral manager's financial condition. At deal inception, the Company typically is not deemed to control a VIE; however, once a trigger event occurs, the Company's control of the VIE typically increases. The Company continuously evaluates its power to direct the activities that most significantly impact the economic

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performance of VIEs that have debt obligations insured by the Company and, accordingly, where the Company is obligated to absorb VIE losses or receive benefits that could potentially be significant to the VIE. The Company obtains protective rights under its insurance contracts that give the Company additional controls over a VIE if there is either deterioration of deal performance or in the financial health of the deal servicer. The Company is deemed to be the control party for certain VIEs under GAAP, typically when its protective rights give it the power to both terminate and replace the deal servicer, which are characteristics specific to the Company's financial guaranty contracts. If the protective rights that could make the Company the control party have not been triggered, then the VIE is not consolidated. If the Company is deemed no longer to have those protective rights, the transaction is deconsolidated.

Number of FG VIEs Consolidated

	Six Months	
	2016	2015
Beginning of the period, December 31	34	32
Radian Asset Acquisition	—	4
Consolidated (1)	—	1
Deconsolidated (1)	(1)	—
Matured	(1)	—
End of the period, June 30	32	37

(1) Net loss on deconsolidation was de minimis in Six Months 2016, and net loss on consolidation was $26 million in Six Months 2015, and recorded in “fair value gains (losses) on FG VIEs” in the consolidated statement of operations.

The total unpaid principal balance for the FG VIEs’ assets that were over 90 days or more past due was approximately $142 million at June 30, 2016 and $154 million at December 31, 2015. The aggregate unpaid principal of the FG VIEs’ assets was approximately $655 million greater than the aggregate fair value at June 30, 2016. The aggregate unpaid principal of the FG VIEs’ assets was approximately $804 million greater than the aggregate fair value at December 31, 2015, excluding the effect of R&W settlements.

The change in the instrument-specific credit risk of the FG VIEs’ assets held as of June 30, 2016 that was recorded in the consolidated statements of operations for Second Quarter 2016 and Six Months 2016 were losses of $3 million and gains of $31 million, respectively. The change in the instrument-specific credit risk of the FG VIEs’ assets held as of June 30, 2015 that was recorded in the consolidated statements of operations for Second Quarter 2015 and Six Months 2015 were losses of $50 million and $32 million, respectively. To calculate the instrument specific credit risk, the changes in the fair value of the FG VIE assets are allocated between changes that are due to the instrument specific credit risk and changes due to other factors, including interest rates. The instrument specific credit risk amount is determined by using expected contractual cash flows versus current expected cash flows discounted at original contractual rate. The net present value is calculated by discounting the expected cash flows of the underlying security, excluding the Company’s financial guaranty insurance, at the relevant effective interest rate.

The unpaid principal for FG VIE liabilities with recourse, which represent obligations insured by AGC or AGM, was $885 million and $1,436 million as of June 30, 2016 and December 31, 2015, respectively. FG VIE liabilities with recourse will mature at various dates ranging from 2025 to 2038. The aggregate unpaid principal balance of the FG VIE liabilities with and without recourse was approximately $287 million greater than the aggregate fair value of the FG VIEs’ liabilities as of June 30, 2016. The aggregate unpaid principal balance was approximately $423 million greater than the aggregate fair value of the FG VIEs' liabilities as of December 31, 2015.

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The table below shows the carrying value of the consolidated FG VIEs' assets and liabilities in the consolidated financial statements, segregated by the types of assets that collateralize their respective debt obligations for FG VIE liabilities with recourse.

Consolidated FG VIEs
By Type of Collateral

	As of June 30, 2016		As of December 31, 2015	
	Assets	Liabilities	Assets	Liabilities
	(in millions)			
With recourse:				
U.S. RMBS first lien	$442	$ 477	$506	$ 521
U.S. RMBS second lien	174	235	194	273
Life insurance	—	—	347	347
Manufactured housing	78	78	84	84
Total with recourse	694	790	1,131	1,225
Without recourse	120	115	130	124
Total	$814	$ 905	$1,261	$ 1,349

The consolidation of FG VIEs has a significant effect on net income and shareholders' equity due to (i) changes in fair value gains (losses) on FG VIE assets and liabilities, (ii) the elimination of premiums and losses related to the AGC and AGM FG VIE liabilities with recourse and (iii) the elimination of investment balances related to the Company's purchase of AGC and AGM insured FG VIE debt. Upon consolidation of a FG VIE, the related insurance and, if applicable, the related investment balances, are considered intercompany transactions and therefore eliminated. Such eliminations are included in the table below to present the full effect of consolidating FG VIEs.

Effect of Consolidating FG VIEs on Net Income,
Cash Flows From Operating Activities and Shareholders' Equity

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Net earned premiums	$(3)	$(5)	$(8)	$(10)
Net investment income	(2)	(3)	(7)	(6)
Net realized investment gains (losses)	0	3	1	3
Fair value gains (losses) on FG VIEs	4	5	22	(2)
Bargain purchase gain	—	2	—	2
Loss and LAE	(2)	2	4	7
Effect on income before tax	(3)	4	12	(6)
Less: tax provision (benefit)	(1)	1	4	(3)
Effect on net income (loss)	$(2)	$3	$8	$(3)
Effect on cash flows from operating activities	$(1)	$15	$5	$33

	As of June	As of December

	30, 2016	31, 2015
	(in millions)	
Effect on shareholders' equity (decrease) increase	$(12)	$ (23)

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Fair value gains (losses) on FG VIEs represent the net change in fair value on the consolidated FG VIEs' assets and liabilities. During Second Quarter and Six Months 2016, the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of $4 million and $22 million respectively. The primary driver of the gains was mark-to-market gains due to price appreciation on the FG VIE assets during the quarter and six months period resulting from improvements in the underlying collateral.

During Second Quarter 2015, the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of $5 million. The primary driver of the gain was mark-to-market gains due to price appreciation on the FG VIE assets during the quarter resulting from improvements in the underlying collateral. During Six Months 2015, the Company recorded a pre-tax net fair value loss on consolidated FG VIEs of $2 million. The primary driver of the loss was a pre-tax loss of $26 million on the consolidation of one new FG VIE which was partially offset by net mark-to-market gains due to price appreciation on the FG VIE assets resulting from improvements in the underlying collateral.

Other Consolidated VIEs

In certain instances where the Company consolidates a VIE that was established as part of a loss mitigation negotiation settlement agreement that results in the termination of the original insured financial guaranty insurance or credit derivative contract the Company classifies the assets and liabilities of those VIEs in the line items that most accurately reflect the nature of the items, as opposed to within the FG VIE assets and FG VIE liabilities.

Non-Consolidated VIEs

As of June 30, 2016 and December 31, 2015, the Company had financial guaranty contracts outstanding for approximately 670 and 750 VIEs, respectively, that it did not consolidate. To date, the Company's analyses have indicated that it does not have a controlling financial interest in any other VIEs and, as a result, they are not consolidated. The Company's exposure provided through its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 4, Outstanding Exposure.

10. Investments and Cash

Net Investment Income and Realized Gains (Losses)

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. Accrued investment income, which is recorded in Other Assets, was $89 million and $99 million as of June 30, 2016 and December 31, 2015, respectively.

Net Investment Income

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Income from fixed-maturity securities managed by third parties	$77	$85	$156	$167
Income from internally managed securities:				
Fixed maturities	22	14	39	29
Other	1	1	6	7
Gross investment income	100	100	201	203
Investment expenses	(2)	(2)	(4)	(4)

Net investment income	$98	$98	$197	$199

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Net Realized Investment Gains (Losses)

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Gross realized gains on available-for-sale securities	$14	$8	$20	$32
Gross realized losses on available-for-sale securities	0	(6)	(2)	(7)
Net realized gains (losses) on other invested assets	1	1	0	1
Other-than-temporary impairment	(5)	(12)	(21)	(19)
Net realized investment gains (losses)	$10	$(9)	$(3)	$7

The following table presents the roll-forward of the credit losses of fixed-maturity securities for which the Company has recognized an other-than-temporary-impairment and where the portion of the fair value adjustment related to other factors was recognized in other comprehensive income ("OCI").

Roll Forward of Credit Losses
in the Investment Portfolio

	Second Quarter		Six Months	
	2016	2015	2016	2015
	(in millions)			
Balance, beginning of period	$107	$106	$108	$124
Additions for credit losses on securities for which an other-than-temporary-impairment was not previously recognized	0	0	2	0
Reductions for securities sold and other settlement during the period	(2)	(7)	(4)	(28)
Additions for credit losses on securities for which an other-than-temporary-impairment was previously recognized	3	5	2	8
Balance, end of period	$108	$104	$108	$104

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Investment Portfolio

Fixed-Maturity Securities and Short-Term Investments
by Security Type
As of June 30, 2016

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI(2) Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Rating(3)
		(dollars in millions)					
Fixed-maturity securities:							
Obligations of state and political subdivisions	52 %	$ 5,143	$ 461	$ (1)	$ 5,603	$ 17	AA-
U.S. government and agencies	3	299	27	0	326	—	AA+
Corporate securities	14	1,402	79	(38)	1,443	(29)	A-
Mortgage-backed securities(4):	0						
RMBS	10	1,037	44	(19)	1,062	(9)	A
CMBS	5	505	34	0	539	—	AAA
Asset-backed securities	7	745	2	(17)	730	(15)	B+
Foreign government securities	3	270	5	(18)	257	—	AA
Total fixed-maturity securities	94	9,401	652	(93)	9,960	(36)	A+
Short-term investments	6	585	0	0	585	—	AAA
Total investment portfolio	100 %	$ 9,986	$ 652	$ (93)	$ 10,545	$ (36)	A+

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Fixed-Maturity Securities and Short-Term Investments
by Security Type
As of December 31, 2015

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI Gain (Loss) on Securities with Other-Than-Temporary Impairment	Weighted Average Credit Rating(3)
		(dollars in millions)					
Fixed-maturity securities:							
Obligations of state and political subdivisions	52 %	$ 5,528	$ 323	$ (10)	$ 5,841	$ 5	AA
U.S. government and agencies	3	377	23	0	400	—	AA+
Corporate securities	14	1,505	38	(23)	1,520	(13)	A-
Mortgage-backed securities(4):							
RMBS	11	1,238	29	(22)	1,245	(7)	A
CMBS	5	506	9	(2)	513	—	AAA
Asset-backed securities	8	831	4	(10)	825	(6)	B+
Foreign government securities	3	290	4	(11)	283	—	AA+
Total fixed-maturity securities	96	10,275	430	(78)	10,627	(21)	A+
Short-term investments	4	396	0	0	396	—	AA-
Total investment portfolio	100%	$ 10,671	$ 430	$ (78)	$ 11,023	$ (21)	A+

(1) Based on amortized cost.

(2) Accumulated OCI. See also Note 17, Shareholders' Equity for additional information as applicable.

(3) Ratings in the tables above represent the lower of the Moody’s and S&P classifications except for bonds purchased for loss mitigation or risk management strategies, which use internal ratings classifications. The Company’s portfolio consists primarily of high-quality, liquid instruments.

(4) Government-agency obligations were approximately 47% of mortgage backed securities as of June 30, 2016 and 54% as of December 31, 2015 based on fair value.

The Company’s investment portfolio in tax-exempt and taxable municipal securities includes issuances by a wide number of municipal authorities across the U.S. and its territories. Under the Company's investment guidelines, securities rated lower than A-/A3 by S&P or Moody’s are typically not purchased for the Company’s portfolio unless acquired for loss mitigation or risk management strategies.

The majority of the investment portfolio is managed by four outside managers. The Company has established detailed guidelines regarding credit quality, exposure to a particular sector and exposure to a particular obligor within a sector.

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The following tables summarize, for all fixed-maturity securities in an unrealized loss position, the aggregate fair value and gross unrealized loss by length of time the amounts have continuously been in an unrealized loss position.

Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of June 30, 2016

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
	(dollars in millions)					
Obligations of state and political subdivisions	$25	$ 0	$ 10	$ (1)	$35	$ (1)
U.S. government and agencies	10	0	—	—	10	0
Corporate securities	54	(5)	81	(33)	135	(38)
Mortgage-backed securities:						
RMBS	47	(5)	115	(14)	162	(19)
CMBS	7	0	—	—	7	0
Asset-backed securities	543	(17)	—	—	543	(17)
Foreign government securities	84	(9)	52	(9)	136	(18)
Total	$770	$ (36)	$ 258	$ (57)	$1,028	$ (93)
Number of securities (1)		68		53		113
Number of securities with other-than-temporary impairment (1)		8		7		14

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Fixed-Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2015

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
	(dollars in millions)					
Obligations of state and political subdivisions	$316	$ (10)	$ 7	$ 0	$323	$ (10)
U.S. government and agencies	77	0	—	—	77	0
Corporate securities	381	(8)	95	(15)	476	(23)
Mortgage-backed securities:						
RMBS	438	(8)	90	(14)	528	(22)
CMBS	140	(2)	2	0	142	(2)
Asset-backed securities	517	(10)	—	—	517	(10)
Foreign government securities	97	(4)	82	(7)	179	(11)
Total	$1,966	$ (42)	$ 276	$ (36)	$2,242	$ (78)
Number of securities (1)		335		71		396
Number of securities with other-than-temporary impairment		9		4		13

(1) The number of securities does not add across because lots consisting of the same securities have been purchased at different times and appear in both categories above (i.e., less than 12 months and 12 months or more). If a security appears in both categories, it is counted only once in the total column.

Of the securities in an unrealized loss position for 12 months or more as of June 30, 2016, 26 securities had unrealized losses greater than 10% of book value. The total unrealized loss for these securities as of June 30, 2016 was $55 million. As of December 31, 2015, of the securities in an unrealized loss position for 12 months or more, nine securities had unrealized losses greater than 10% of book value with unrealized loss amount of $26 million. The Company has determined that the unrealized losses recorded as of June 30, 2016 and December 31, 2015 were yield related and not the result of other-than-temporary-impairment.

The amortized cost and estimated fair value of available-for-sale fixed maturity securities by contractual maturity as of June 30, 2016 are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Distribution of Fixed-Maturity Securities
by Contractual Maturity
As of June 30, 2016

	Amortized Cost	Estimated Fair Value
	(in millions)	
Due within one year	$482	$ 484
Due after one year through five years	1,484	1,536
Due after five years through 10 years	1,926	2,066
Due after 10 years	3,967	4,273
Mortgage-backed securities:		
RMBS	1,037	1,062

CMBS	505	539
Total	$9,401	$ 9,960

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The investment portfolio contains securities and cash that are either held in trust for the benefit of third party reinsurers in accordance with statutory requirements, invested in a guaranteed investment contract for future claims payments, placed on deposit to fulfill state licensing requirements, or otherwise restricted in the amount of $300 million and $283 million as of June 30, 2016 and December 31, 2015, respectively, based on fair value. The investment portfolio also contains securities that are held in trust by certain AGL subsidiaries for the benefit of other AGL subsidiaries in accordance with statutory and regulatory requirements in the amount of $1,561 million and $1,411 million as of June 30, 2016 and December 31, 2015, respectively, based on fair value.

The fair value of the Company’s pledged securities to secure its obligations under its CDS exposure totaled $216 million and $305 million as of June 30, 2016 and December 31, 2015, respectively.

No material investments of the Company were non-income producing for Six Months 2016 and Six Months 2015, respectively.

Internally Managed Portfolio

The investment portfolio tables shown above include both assets managed externally and internally. In the table below, more detailed information is provided for the component of the total investment portfolio that is internally managed (excluding short-term investments). The internally managed portfolio, as defined below, represents approximately 13% and 13% of the investment portfolio, on a fair value basis as of June 30, 2016 and December 31, 2015, respectively. The internally managed portfolio consists primarily of the Company's investments in securities for (i) loss mitigation purposes, (ii) other risk management purposes and (iii) where the Company believes a particular security presents an attractive investment opportunity.

One of the Company's strategies for mitigating losses has been to purchase securities it has insured that have expected losses, at discounted prices (assets purchased for loss mitigation purposes). In addition, the Company holds other invested assets that were obtained or purchased as part of negotiated settlements with insured counterparties or under the terms of our financial guaranties (other risk management assets).

Internally Managed Portfolio
Carrying Value

	As of June 30, 2016	As of December 31, 2015
	(in millions)	
Assets purchased for loss mitigation and other risk management purposes:		
Fixed-maturity securities, at fair value	$1,208	$ 1,266
Other invested assets	113	114
Other	58	55
Total	$1,379	$ 1,435

11. Insurance Company Regulatory Requirements

Dividend Restrictions and Capital Requirements

Under New York insurance law, AGM may only pay dividends out of "earned surplus," which is the portion of the company's surplus that represents the net earnings, gains or profits (after deduction of all losses) that have not been distributed to shareholders as dividends or transferred to stated capital or capital surplus, or applied to other purposes permitted by law, but does not include unrealized appreciation of assets. AGM may pay dividends without the prior approval of the New York Superintendent of Financial Services ("New York Superintendent") that, together with all dividends declared or distributed by it during the preceding 12 months, does not exceed the lesser of 10% of its policyholders' surplus (as of its last annual or quarterly statement filed with the New York Superintendent) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGM to distribute as dividends without regulatory approval is estimated to be approximately $244 million, of which approximately $65 million is estimated to be available for distribution in the third quarter of 2016.

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Under Maryland's insurance law, AGC may, with prior notice to the Maryland Insurance Commissioner, pay an ordinary dividend that, together with all dividends paid in the prior 12 months, does not exceed the lesser of 10% of its policyholders' surplus (as of the prior December 31) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGC to distribute as ordinary dividends is approximately $79 million, of which approximately $16 million is available for distribution in the third quarter of 2016.

MAC is a New York domiciled insurance company subject to the same dividend limitations described above for AGM. The Company does not currently anticipate that MAC will distribute any dividends. On June 30, 2016, MAC obtained approval from the New York State Department of Financial Services to repay its $300 million surplus note to Municipal Assurance Holdings Inc. ("MAC Holdings") and its $100 million surplus note (plus accrued interest) to AGM. Accordingly, on June 30, 2016, MAC transferred cash and/or marketable securities to (i) MAC Holdings in an aggregate amount equal to $300 million, and (ii) AGM in an aggregate amount of $102.5 million. MAC Holdings, upon receipt of such $300 million from MAC, distributed cash and/or marketable securities in an aggregate amount of $300 million to its shareholders, AGM and AGC, in proportion to their respective