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).

ASSURED GUARANTY LTD.

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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
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(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

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(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

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 (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

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(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

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(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%	

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(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.

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.

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

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(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				
	Gross	Ceded	Gross	Ceded	Gross	Ceded	Total BIG, Net	Effect of Consolidating FG VIEs	Total
	(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)	204	(26	85	(13	132	(44	419	—	419
Remaining weighted-average contract period (in years)	10.0								