

ASSURED GUARANTY LTD

Form 10-Q

May 05, 2016

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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FORM 10-Q

ý QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period Ended March 31, 2016

Or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
o 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 (I.R.S. employer  
of incorporation) 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

Smaller reporting company o

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

The number of registrant's Common Shares (\$0.01 par value) outstanding as of May 2, 2016 was 134,357,143 (includes 62,145 unvested restricted shares).

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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

Assured Guaranty Ltd.

Consolidated Balance Sheets (unaudited)

(dollars in millions except per share and share amounts)

|                                                                                                                           | As of<br>March<br>31,<br>2016 | As of<br>December<br>31, 2015 |
|---------------------------------------------------------------------------------------------------------------------------|-------------------------------|-------------------------------|
| Assets                                                                                                                    |                               |                               |
| Investment portfolio:                                                                                                     |                               |                               |
| Fixed-maturity securities, available-for-sale, at fair value (amortized cost of \$10,123 and \$10,275)                    | \$10,588                      | \$ 10,627                     |
| Short-term investments, at fair value                                                                                     | 459                           | 396                           |
| Other invested assets                                                                                                     | 167                           | 169                           |
| Total investment portfolio                                                                                                | 11,214                        | 11,192                        |
| Cash                                                                                                                      | 112                           | 166                           |
| Premiums receivable, net of commissions payable                                                                           | 662                           | 693                           |
| Ceded unearned premium reserve                                                                                            | 236                           | 232                           |
| Deferred acquisition costs                                                                                                | 113                           | 114                           |
| Reinsurance recoverable on unpaid losses                                                                                  | 72                            | 69                            |
| Salvage and subrogation recoverable                                                                                       | 206                           | 126                           |
| Credit derivative assets                                                                                                  | 55                            | 81                            |
| Deferred tax asset, net                                                                                                   | 278                           | 276                           |
| Current income tax receivable                                                                                             | 11                            | 40                            |
| Financial guaranty variable interest entities' assets, at fair value                                                      | 1,191                         | 1,261                         |
| Other assets                                                                                                              | 302                           | 294                           |
| Total assets                                                                                                              | \$14,452                      | \$ 14,544                     |
| Liabilities and shareholders' equity                                                                                      |                               |                               |
| Unearned premium reserve                                                                                                  | \$3,810                       | \$ 3,996                      |
| Loss and loss adjustment expense reserve                                                                                  | 1,112                         | 1,067                         |
| Reinsurance balances payable, net                                                                                         | 58                            | 51                            |
| Long-term debt                                                                                                            | 1,302                         | 1,300                         |
| Credit derivative liabilities                                                                                             | 489                           | 446                           |
| Financial guaranty variable interest entities' liabilities with recourse, at fair value                                   | 1,165                         | 1,225                         |
| Financial guaranty variable interest entities' liabilities without recourse, at fair value                                | 119                           | 124                           |
| Other liabilities                                                                                                         | 284                           | 272                           |
| Total liabilities                                                                                                         | 8,339                         | 8,481                         |
| Commitments and contingencies (See Note 14)                                                                               |                               |                               |
| Common stock (\$0.01 par value, 500,000,000 shares authorized; 135,083,637 and 137,928,552 shares issued and outstanding) | 1                             | 1                             |
| Additional paid-in capital                                                                                                | 1,269                         | 1,342                         |
| Retained earnings                                                                                                         | 4,519                         | 4,478                         |
| Accumulated other comprehensive income, net of tax of \$127 and \$104                                                     | 319                           | 237                           |
| Deferred equity compensation (320,193 and 320,193 shares)                                                                 | 5                             | 5                             |
| Total shareholders' equity                                                                                                | 6,113                         | 6,063                         |

|                                            |           |           |
|--------------------------------------------|-----------|-----------|
| Total liabilities and shareholders' equity | \$ 14,452 | \$ 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<br>Ended March<br>31, |        |
|---------------------------------------------------------------------------------------------------|------------------------------------|--------|
|                                                                                                   | 2016                               | 2015   |
| Revenues                                                                                          |                                    |        |
| Net earned premiums                                                                               | \$183                              | \$142  |
| Net investment income                                                                             | 99                                 | 101    |
| Net realized investment gains (losses):                                                           |                                    |        |
| Other-than-temporary impairment losses                                                            | (20 )                              | (5 )   |
| Less: portion of other-than-temporary impairment loss<br>recognized in other comprehensive income | (4 )                               | 2      |
| Net impairment loss                                                                               | (16 )                              | (7 )   |
| Other net realized investment gains (losses)                                                      | 3                                  | 23     |
| Net realized investment gains (losses)                                                            | (13 )                              | 16     |
| Net change in fair value of credit derivatives:                                                   |                                    |        |
| Realized gains (losses) and other settlements                                                     | 8                                  | 21     |
| Net unrealized gains (losses)                                                                     | (68 )                              | 103    |
| Net change in fair value of credit derivatives                                                    | (60 )                              | 124    |
| Fair value gains (losses) on committed capital securities                                         | (16 )                              | 2      |
| Fair value gains (losses) on financial guaranty variable interest entities                        | 18                                 | (7 )   |
| Other income (loss)                                                                               | 34                                 | (9 )   |
| Total revenues                                                                                    | 245                                | 369    |
| Expenses                                                                                          |                                    |        |
| Loss and loss adjustment expenses                                                                 | 90                                 | 18     |
| Amortization of deferred acquisition costs                                                        | 4                                  | 4      |
| Interest expense                                                                                  | 26                                 | 25     |
| Other operating expenses                                                                          | 60                                 | 56     |
| Total expenses                                                                                    | 180                                | 103    |
| Income (loss) before income taxes                                                                 | 65                                 | 266    |
| Provision (benefit) for income taxes                                                              |                                    |        |
| Current                                                                                           | 30                                 | 13     |
| Deferred                                                                                          | (24 )                              | 52     |
| Total provision (benefit) for income taxes                                                        | 6                                  | 65     |
| Net income (loss)                                                                                 | \$59                               | \$201  |
| Earnings per share:                                                                               |                                    |        |
| Basic                                                                                             | \$0.43                             | \$1.29 |
| Diluted                                                                                           | \$0.43                             | \$1.28 |
| Dividends per share                                                                               | \$0.13                             | \$0.12 |

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<br>Months<br>Ended March<br>31, |       |
|-------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------|-------|
|                                                                                                                                     | 2016                                  | 2015  |
| Net income (loss)                                                                                                                   | \$59                                  | \$201 |
| Unrealized holding gains (losses) arising during the period on:                                                                     |                                       |       |
| Investments with no other-than-temporary impairment, net of tax provision (benefit) of \$31, and \$1                                | 95                                    | 18    |
| Investments with other-than-temporary impairment, net of tax provision (benefit) of \$(10) and \$(2)                                | (17 )                                 | (2 )  |
| Unrealized holding gains (losses) arising during the period, net of tax                                                             | 78                                    | 16    |
| Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of \$(4) and \$6 | (6 )                                  | 10    |
| Change in net unrealized gains on investments                                                                                       | 84                                    | 6     |
| Other, net of tax provision                                                                                                         | (2 )                                  | (6 )  |
| Other comprehensive income (loss)                                                                                                   | \$82                                  | \$0   |
| Comprehensive income (loss)                                                                                                         | \$141                                 | \$201 |

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 Three Months Ended March 31, 2016

(dollars in millions, except share data)

|                                    | Common<br>Shares<br>Outstanding | Common Stock<br>Par Value | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income | Deferred<br>Equity<br>Compensation | Total<br>Shareholders'<br>Equity |
|------------------------------------|---------------------------------|---------------------------|----------------------------------|----------------------|-------------------------------------------------|------------------------------------|----------------------------------|
| Balance at December 31, 2015       | 137,928,552                     | \$ 1                      | \$ 1,342                         | \$ 4,478             | \$ 237                                          | \$ 5                               | \$ 6,063                         |
| Net income                         | —                               | —                         | —                                | 59                   | —                                               | —                                  | 59                               |
| Dividends (\$0.13 per share)       | —                               | —                         | —                                | (18 )                | —                                               | —                                  | (18 )                            |
| Common stock repurchases           | (3,038,928 )                    | 0                         | (75 )                            | —                    | —                                               | —                                  | (75 )                            |
| Share-based compensation and other | 194,013                         | 0                         | 2                                | —                    | —                                               | —                                  | 2                                |
| Other comprehensive income         | —                               | —                         | —                                | —                    | 82                                              | —                                  | 82                               |
| Balance at March 31, 2016          | 135,083,637                     | \$ 1                      | \$ 1,269                         | \$ 4,519             | \$ 319                                          | \$ 5                               | \$ 6,113                         |

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)

|                                                                                     | Three<br>Months<br>Ended March<br>31,<br>2016 2015 |        |
|-------------------------------------------------------------------------------------|----------------------------------------------------|--------|
| Net cash flows provided by (used in) operating activities                           | \$(90 )                                            | \$23   |
| Investing activities                                                                |                                                    |        |
| Fixed-maturity securities:                                                          |                                                    |        |
| Purchases                                                                           | (296 )                                             | (448 ) |
| Sales                                                                               | 162                                                | 841    |
| Maturities                                                                          | 301                                                | 155    |
| Net sales (purchases) of short-term investments                                     | (63 )                                              | 420    |
| Net proceeds from paydowns on financial guaranty variable interest entities' assets | 66                                                 | 30     |
| Other                                                                               | 2                                                  | 3      |
| Net cash flows provided by (used in) investing activities                           | 172                                                | 1,001  |
| Financing activities                                                                |                                                    |        |
| Dividends paid                                                                      | (18 )                                              | (19 )  |
| Repurchases of common stock                                                         | (75 )                                              | (152 ) |
| Share activity under option and incentive plans                                     | 0                                                  | (5 )   |
| Net paydowns of financial guaranty variable interest entities' liabilities          | (42 )                                              | (39 )  |
| Repayment of long-term debt                                                         | 0                                                  | (1 )   |
| Other                                                                               | (1 )                                               | 4      |
| Net cash flows provided by (used in) financing activities                           | (136 )                                             | (212 ) |
| Effect of foreign exchange rate changes                                             | 0                                                  | (2 )   |
| Increase (decrease) in cash                                                         | (54 )                                              | 810    |
| Cash at beginning of period                                                         | 166                                                | 75     |
| Cash at end of period                                                               | \$112                                              | \$885  |
| Supplemental cash flow information                                                  |                                                    |        |
| Cash paid (received) during the period for:                                         |                                                    |        |
| Income taxes                                                                        | \$1                                                | \$17   |
| Interest                                                                            | \$7                                                | \$7    |

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)

March 31, 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 March 31, 2016 and cover the three-month period ended March 31, 2016 ("First Quarter 2016") and the three-month period ended March 31, 2015 ("First Quarter 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

### Share-Based Payments

In March 2016, the Financial Accounting Standards Board issued Accounting Standards Update ("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 of adopting this ASU on its Consolidated Financial Statements.

## 2. Acquisitions

Consistent with one of its key business strategies of supplementing its book of business through acquisitions, the Company has acquired or agreed to acquire two financial guaranty companies within the last 12 months.

### CIFG Holding Inc.

On April 12, 2016, AGC entered into an agreement and plan of merger to acquire CIFG Holding Inc. ("CIFG"), the parent of financial guaranty insurer CIFG Assurance North America, Inc. ("CIFG NA"). AGC expects to pay \$450 million in cash to acquire CIFG, subject to adjustments as contemplated in the agreement, and the acquisition is expected to be completed mid-2016, subject to receipt of anti-trust and insurance regulatory approvals as well as satisfaction of customary closing conditions. CIFG's stockholders have already approved the acquisition. As part of the transaction, CIFG NA will merge into AGC, which will be the surviving entity. As of December 31, 2015, CIFG had a consolidated insured portfolio of \$5.6 billion of net par and approximately \$637 million of consolidated qualified statutory capital.

### Radian Asset Assurance Inc.

On April 1, 2015 ("Acquisition Date"), 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.

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### 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 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.

On August 3, 2015 and December 10, 2015, KBRA affirmed the AA+ (stable outlook) financial strength ratings of MAC and AGM, respectively.

On June 29, 2015, S&P affirmed the AA (stable) financial strength ratings of all of AGL's insurance subsidiaries.

On May 5, 2015, Best assigned to AGRO a financial strength rating of A+ (Stable), which is their second highest rating.

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.

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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 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.

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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<br>Outstanding |            | Net Debt Service<br>Outstanding |            |
|--------------------------|-----------------------------------|------------|---------------------------------|------------|
|                          | March 31, December 31,            |            | March 31, December 31,          |            |
|                          | 2016                              | 2015       | 2016                            | 2015       |
|                          | (in millions)                     |            |                                 |            |
| Public finance           | \$496,630                         | \$ 515,494 | \$476,362                       | \$ 494,426 |
| Structured finance       | 42,012                            | 43,976     | 40,037                          | 41,915     |
| Total financial guaranty | \$538,642                         | \$ 559,470 | \$516,399                       | \$ 536,341 |

In addition to the amounts shown in the table above, the Company's net mortgage guaranty insurance debt service was approximately \$107 million as of March 31, 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.

## Financial Guaranty Portfolio by Internal Rating

As of March 31, 2016

| Rating<br>Category               | Public Finance<br>U.S. |        |   | Public Finance<br>Non-U.S. |        |   | Structured Finance<br>U.S |        |   | Structured Finance<br>Non-U.S |        |   | Total       |        |   |
|----------------------------------|------------------------|--------|---|----------------------------|--------|---|---------------------------|--------|---|-------------------------------|--------|---|-------------|--------|---|
|                                  | Net Par                |        |   | Net Par                    |        |   | Net Par                   |        |   | Net Par                       |        |   | Net Par     |        |   |
|                                  | Outstanding            |        |   | Outstanding                |        |   | Outstanding               |        |   | Outstanding                   |        |   | Outstanding |        |   |
|                                  | %                      |        |   | %                          |        |   | %                         |        |   | %                             |        |   | %           |        |   |
| (dollars in millions)            |                        |        |   |                            |        |   |                           |        |   |                               |        |   |             |        |   |
| AAA                              | \$2,541                | 0.9    | % | \$688                      | 2.3    | % | \$13,953                  | 45.8   | % | \$2,529                       | 49.4   | % | \$19,711    | 5.7    | % |
| AA                               | 65,310                 | 23.2   |   | 1,969                      | 6.7    |   | 7,505                     | 24.7   |   | 154                           | 3.0    |   | 74,938      | 21.6   |   |
| A                                | 145,515                | 51.6   |   | 6,695                      | 22.8   |   | 2,584                     | 8.5    |   | 551                           | 10.8   |   | 155,345     | 44.7   |   |
| BBB                              | 60,736                 | 21.5   |   | 18,622                     | 63.4   |   | 1,279                     | 4.2    |   | 1,267                         | 24.7   |   | 81,904      | 23.6   |   |
| BIG                              | 7,953                  | 2.8    |   | 1,411                      | 4.8    |   | 5,131                     | 16.8   |   | 622                           | 12.1   |   | 15,117      | 4.4    |   |
| Total net par<br>outstanding (1) | \$282,055              | 100.0% |   | \$29,385                   | 100.0% |   | \$30,452                  | 100.0% |   | \$5,123                       | 100.0% |   | \$347,015   | 100.0% |   |

(1) Excludes \$1.5 billion of loss mitigation securities insured and held by the Company as of March 31, 2016, which are primarily BIG.

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## Financial Guaranty Portfolio by Internal Rating

As of December 31, 2015

| Rating<br>Category               | Public Finance<br>U.S. |        |                  | Public Finance<br>Non-U.S. |        |                  | Structured Finance<br>U.S |        |                  | Structured Finance<br>Non-U.S |        |                  | Total     |        |                  |
|----------------------------------|------------------------|--------|------------------|----------------------------|--------|------------------|---------------------------|--------|------------------|-------------------------------|--------|------------------|-----------|--------|------------------|
|                                  | Net Par                |        | %<br>Outstanding | Net Par                    |        | %<br>Outstanding | Net Par                   |        | %<br>Outstanding | Net Par                       |        | %<br>Outstanding | Net Par   |        | %<br>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<br>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 \$240 million for public finance obligations as of March 31, 2016. The expiration dates for the public finance commitments range between April 1, 2016 and February 25, 2017, with \$66 million expiring prior to the date of this filing and an additional \$110 million expiring prior to December 31, 2016. 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.

## Components of BIG Portfolio

## Components of BIG Net Par Outstanding

(Insurance and Credit Derivative Form)

As of March 31, 2016

|                                                                  | BIG Net Par Outstanding |         |        | Total BIG | Net Par<br>Outstanding |
|------------------------------------------------------------------|-------------------------|---------|--------|-----------|------------------------|
|                                                                  | BIG 1                   | BIG 2   | BIG 3  |           |                        |
|                                                                  | (in millions)           |         |        |           |                        |
| U.S. public finance                                              | \$4,608                 | \$3,191 | \$ 154 | \$ 7,953  | \$ 282,055             |
| Non-U.S. public finance                                          | 882                     | 529     | —      | 1,411     | 29,385                 |
| Structured finance:                                              |                         |         |        |           |                        |
| First lien U.S. residential mortgage-backed securities ("RMBS"): |                         |         |        |           |                        |
| Prime first lien                                                 | 192                     | 32      | 24     | 248       | 425                    |
| Alt-A first lien                                                 | 125                     | 66      | 507    | 698       | 1,238                  |
| Option ARM                                                       | 50                      | 7       | 78     | 135       | 235                    |
| Subprime                                                         | 82                      | 281     | 866    | 1,229     | 3,305                  |
| Second lien U.S. RMBS                                            | 225                     | 47      | 1,100  | 1,372     | 1,474                  |
| Total U.S. RMBS                                                  | 674                     | 433     | 2,575  | 3,682     | 6,677                  |
| Triple-X life insurance transactions                             | —                       | —       | 216    | 216       | 2,650                  |
| Trust preferred securities ("TruPS")                             | 650                     | 127     | —      | 777       | 4,296                  |
| Student loans                                                    | —                       | 68      | 81     | 149       | 1,815                  |
| Other structured finance                                         | 743                     | 147     | 39     | 929       | 20,137                 |

|       |         |         |          |           |            |
|-------|---------|---------|----------|-----------|------------|
| Total | \$7,557 | \$4,495 | \$ 3,065 | \$ 15,117 | \$ 347,015 |
|-------|---------|---------|----------|-----------|------------|

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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  |

BIG Net Par Outstanding  
and Number of Risks  
As of March 31, 2016

| Description | Net Par Outstanding                   |                             |          | Number of Risks(2)                    |                             |       |
|-------------|---------------------------------------|-----------------------------|----------|---------------------------------------|-----------------------------|-------|
|             | Financial<br>Guaranty<br>Insurance(1) | Credit<br>Derivative<br>(1) | Total    | Financial<br>Guaranty<br>Insurance(1) | Credit<br>Derivative<br>(1) | Total |
|             | (dollars in millions)                 |                             |          |                                       |                             |       |
| BIG:        |                                       |                             |          |                                       |                             |       |
| Category 1  | \$6,585                               | \$ 972                      | \$7,557  | 202                                   | 12                          | 214   |
| Category 2  | 4,015                                 | 480                         | 4,495    | 86                                    | 7                           | 93    |
| Category 3  | 2,938                                 | 127                         | 3,065    | 129                                   | 12                          | 141   |
| Total BIG   | \$13,538                              | \$ 1,579                    | \$15,117 | 417                                   | 31                          | 448   |

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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             | Credit     | Total    | Financial          | Credit     | Total |
|             | Guaranty              | Derivative |          | Guaranty           | Derivative |       |
|             | Insurance(1)          | (1)        |          | Insurance(1)       | (1)        |       |
|             | (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.

#### Exposure to Puerto Rico

The Company has insured exposure to 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 March 31, 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.

In June 2014, the Puerto Rico legislature passed the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (the "Recovery Act") in order to provide a legislative framework for certain public corporations experiencing severe financial stress to restructure their debt, including Puerto Rico Highway and Transportation Authority ("PRHTA") and Puerto Rico Electric Power Authority ("PREPA"). Subsequently, the Commonwealth stated PREPA might need to seek relief under the Recovery Act due to liquidity constraints. Investors in bonds issued by PREPA filed suit in the United States District Court for the District of Puerto Rico challenging the Recovery Act. On February 6, 2015, the U.S. District Court for the District of Puerto Rico ruled the Recovery Act is preempted by the U.S. Bankruptcy Code and is therefore void. On July 6, 2015, the U.S. Court of Appeals for the First Circuit upheld that ruling, and on December 4, 2015, the U.S. Supreme Court granted petitions for writs of certiorari relating to that ruling. Oral arguments were held on March 22, 2016. Typical Supreme Court practice suggests a decision could be announced in June 2016, but there is no assurance that an opinion will be announced at such time, especially in light of the Supreme Court vacancy.

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, is unpayable and that a comprehensive debt restructuring may be necessary, and he has made similar statements since then.

On September 9, 2015, the Working Group for the Fiscal and Economic Recovery of Puerto Rico ("Working Group") established by the Governor published its "Puerto Rico Fiscal and Economic Growth Plan" (the "FEGP"). The FEGP included a recommendation that the Commonwealth's advisors begin to work on a voluntary exchange offer to its



creditors as part of the FEGP.

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 PRHTA, 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 impacted by the Clawback Orders are shown in the table “Puerto Rico Net Par Outstanding” below.

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On January 1, 2016 Puerto Rico Infrastructure Finance Authority ("PRIFA") defaulted on payment of a portion of the interest due on its bonds on that date. For those PRIFA bonds the Company had insured, the Company paid approximately \$451 thousand of claims for the interest payments on which PRIFA had defaulted.

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 a moratorium, entity by entity, on debt service payments on debt of the commonwealth and its related authorities and public corporations, as well as instituting a stay against related litigation, among other things. It is possible that a court may find any attempt to exercise the power to declare a moratorium on debt service payments purportedly granted by the Moratorium Act to be unconstitutional, and the impact of any attempt to exercise such power on the Puerto Rico credits insured by the Company is uncertain. Shortly after signing it into law, the Governor used the authority of the Moratorium Act to declare an emergency period with respect to the Government Development Bank (the "GDB"), placing restrictions on its disbursements and certain of its other activities and moving the clearing of payroll of Commonwealth and GDB employees from the GDB.

On April 30, 2016, the Governor signed an order under the Moratorium Act ordering a moratorium on the debt service payment of approximately \$422 million due to be made by the GDB on May 2, 2016. On May 1, 2016, the GDB announced a tentative agreement with a group of creditors of the GDB (the "Ad Hoc Group") for a restructuring of GDB's notes and that the GDB would pay the interest due on May 2, 2016. According to the announcement, the Ad Hoc Group agreed to forbear from initiating litigation for 30 days during the pendency of negotiations. The GDB noted in its May 1 announcement that the tentative agreement requires 100% participation of the GDB's creditors and that it would be unlikely to reach that level of participation without a restructuring law enabling it to bind non-consenting creditors. The Company does not insure any debt issued by the GDB.

There have been a number of other proposals, plans and legislative initiatives offered in Puerto Rico and in the United States aimed at addressing Puerto Rico's fiscal issues. Among the responses proposed is a federal financial control board and access to bankruptcy courts or another restructuring mechanism. In addition, the Working Group has made several proposals for voluntary exchanges that include terms such as discounts, extensions and subordination. The final shape and timing of responses to Puerto Rico's distress eventually enacted or implemented by Puerto Rico or the United States, if any, and the impact of any such actions on obligations insured by the Company, is uncertain and may differ substantially from the recommendations of the Working Group or any other proposals or plans described in the press or offered to date or in the future.

S&P, Moody's and Fitch Ratings have lowered the credit rating of the Commonwealth's bonds and on its public corporations several times over the past approximately two years, and the Commonwealth has disclosed its liquidity has been adversely affected by rating agency downgrades and by the limited market access for its debt, and also noted it has relied on short-term financings and interim loans from the GDB and other private lenders, which reliance has constrained its liquidity and increased its near-term refinancing risk.

### PREPA

As of March 31, 2016, the Company had \$744 million insured net par outstanding of PREPA obligations. On July 1, 2015, PREPA made full payment of the \$416 million of principal and interest due on its bonds, including bonds insured by AGM and AGC. However, that payment was conditioned on and facilitated by AGM and AGC agreeing, also on July 1, to purchase a portion of \$131 million of interest-bearing bonds to help replenish certain of the operating funds PREPA used to make the \$416 million of principal and interest payments. On July 31, 2015, AGM and AGC purchased \$74 million aggregate principal amount of those bonds; the bonds were repaid in full in 2016.

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, which enables PREPA to achieve debt relief and more efficient capital markets financing, Assured Guaranty will issue surety insurance policies in an aggregate amount not expected to exceed \$113 million in exchange for a market premium and 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. The Company's share of the bridge financing is approximately \$15 million. Legislation meeting the requirements of the RSA was enacted on February 16, 2016. The closing of the restructuring transaction, the issuance of the surety bonds and the closing of the bridge financing are subject

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to certain conditions, including confirmation that the enacted legislation meets all requirements of the RSA and execution of acceptable documentation and legal opinions.

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 restructuring of the insured PREPA revenue bonds, will be implemented. In addition, the impact of 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.

PRHTA

As of March 31, 2016, the Company had \$910 million insured net par outstanding of PRHTA (Transportation revenue) bonds and \$369 million net par of PRHTA (Highway revenue) bonds. 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.

Puerto Rico Sales Tax Financing Corporation ("COFINA")

As of March 31, 2016, the Company had \$270 million insured net par outstanding of junior COFINA bonds, which are secured by a lien on certain sales and use taxes. There have been proposals from both the Commonwealth and from holders of certain senior COFINA bonds to restructure COFINA debt.

Puerto Rico Convention Center District Authority

As of March 31, 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.

Puerto Rico Aqueduct and Sewer Authority ("PRASA")

As of March 31, 2016, the Company had \$388 million insured par outstanding to PRASA bonds, which are secured by the gross revenues of the system. On September 15, 2015, PRASA entered into a settlement with the U.S. Justice Department 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, it owed its contractors \$140 million.

Municipal Finance Agency ("MFA")

As of March 31, 2016, the Company had \$387 million net par outstanding of bonds issued by MFA secured by a pledge of local property tax revenues. On October 13, 2015, the Company filed a motion to intervene in litigation between Centro de Recaudación de Ingresos Municipales ("CRIM") and the GDB in which CRIM was seeking to ensure that the pledged tax revenues are, and will continue to be, available to support the MFA bonds. While the Company's motion to intervene was denied, the GDB and CRIM have reported that they executed a new deed of trust that requires the GDB, as fiduciary, to keep the pledged tax revenues separate from any other GDB monies or accounts and that governs the manner in which the pledged revenues may be invested and dispersed.

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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<br>Outstanding |                      | Gross Debt Service<br>Outstanding |                      |
|---------------------------------------------------|--------------------------|----------------------|-----------------------------------|----------------------|
|                                                   | March 31,<br>2016        | December 31,<br>2015 | March 31,<br>2016                 | December 31,<br>2015 |
|                                                   | (in millions)            |                      |                                   |                      |
| Previously Subject to the Voided Recovery Act (1) | \$2,965                  | \$ 2,965             | \$5,090                           | \$ 5,162             |
| Not Previously Subject to the Voided Recovery Act | 2,791                    | 2,790                | 4,398                             | 4,470                |
| Total                                             | \$5,756                  | \$ 5,755             | \$9,488                           | \$ 9,632             |

(1) On February 6, 2015, the U.S. District Court for the District of Puerto Rico ruled that the Recovery Act is preempted by the U.S. Bankruptcy Code and is therefore void. On July 6, 2015, the U.S. Court of Appeals for the First Circuit upheld that ruling, and on December 4, 2015, the U.S. Supreme Court granted petitions for writs of certiorari relating to that ruling.

Table of ContentsPuerto Rico  
Net Par Outstanding

|                                                              | As of<br>March 31, 2016 |                 | As of<br>December 31, 2015 |                 |
|--------------------------------------------------------------|-------------------------|-----------------|----------------------------|-----------------|
|                                                              | Total                   | Internal Rating | Total                      | Internal Rating |
|                                                              | (in millions)           |                 |                            |                 |
| Exposures Previously Subject to the Voided Recovery Act:     |                         |                 |                            |                 |
| PRHTA (Transportation revenue) (1)                           | \$910                   | CCC-            | \$909                      | CCC-            |
| PREPA                                                        | 744                     | CC              | 744                        | CC              |
| PRASA                                                        | 388                     | CCC             | 388                        | CCC             |
| PRHTA (Highway revenue)(1)                                   | 369                     | CCC             | 370                        | CCC             |
| PRCCDA (1)                                                   | 164                     | CCC-            | 164                        | CCC-            |
| Total                                                        | 2,575                   |                 | 2,575                      |                 |
| Exposures Not Previously Subject to the Voided Recovery Act: |                         |                 |                            |                 |
| Commonwealth of Puerto Rico - General Obligation Bonds       | 1,615                   | CCC             | 1,615                      | CCC             |
| MFA                                                          | 387                     | CCC-            | 387                        | CCC-            |
| COFINA                                                       | 270                     | CCC+            | 269                        | CCC+            |
| Puerto Rico Public Buildings Authority                       | 188                     | CCC             | 188                        | CCC             |
| PRIFA (1) (2)                                                | 18                      | C               | 18                         | CCC-            |
| University of Puerto Rico                                    | 1                       | CCC-            | 1                          | CCC-            |
| Total                                                        | 2,479                   |                 | 2,478                      |                 |
| Total net exposure to Puerto Rico                            | \$5,054                 |                 | \$5,053                    |                 |

The Governor issued executive orders on November 30, 2015, and December 8, 2015, directing the Puerto Rico Department of Treasury and the Puerto Rico Tourism Company to retain or transfer certain taxes and revenues pledged to secure the payment of bonds issued by PRHTA, PRIFA and 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 and revenues is unconstitutional, and demanding declaratory and injunctive relief.

On January 1, 2016 PRIFA defaulted on full payment of a portion of the interest due on its bonds on that date. For those PRIFA bonds the Company had insured, the Company paid approximately \$451 thousand of claims for the interest payments on which PRIFA had defaulted.

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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 March 31, 2016

|                                | Scheduled Net Par<br>Amortization                                                                                                 |          |         | Scheduled Net Debt<br>Service Amortization                                                                       |          |         |
|--------------------------------|-----------------------------------------------------------------------------------------------------------------------------------|----------|---------|------------------------------------------------------------------------------------------------------------------|----------|---------|
|                                | Previously<br>Not<br>Subject Previously<br>to the Subject to<br>Voided the Voided<br>RecoveryRecovery<br>Act Act<br>(in millions) |          | Total   | Previously<br>Not<br>Subject Previously<br>to the Subject to<br>Voided the Voided<br>RecoveryRecovery<br>Act Act |          | Total   |
| 2016 (April 1 – June 30)       | \$0                                                                                                                               | \$ 0     | \$0     | \$2                                                                                                              | \$ 0     | \$2     |
| 2016 (July 1 – September 30)   | 98                                                                                                                                | 204      | 302     | 161                                                                                                              | 267      | 428     |
| 2016 (October 1 – December 31) | 0                                                                                                                                 | 0        | 0       | 2                                                                                                                | 0        | 2       |
| 2017                           | 51                                                                                                                                | 171      | 222     | 175                                                                                                              | 288      | 463     |
| 2018                           | 56                                                                                                                                | 123      | 179     | 178                                                                                                              | 232      | 410     |
| 2019                           | 74                                                                                                                                | 130      | 204     | 192                                                                                                              | 232      | 424     |
| 2020                           | 87                                                                                                                                | 183      | 270     | 202                                                                                                              | 280      | 482     |
| 2021                           | 66                                                                                                                                | 59       | 125     | 177                                                                                                              | 146      | 323     |
| 2022                           | 47                                                                                                                                | 68       | 115     | 153                                                                                                              | 152      | 305     |
| 2023                           | 110                                                                                                                               | 40       | 150     | 214                                                                                                              | 123      | 337     |
| 2024                           | 89                                                                                                                                | 85       | 174     | 188                                                                                                              | 164      | 352     |
| 2025                           | 111                                                                                                                               | 85       | 196     | 206                                                                                                              | 159      | 365     |
| 2026-2030                      | 590                                                                                                                               | 353      | 943     | 974                                                                                                              | 660      | 1,634   |
| 2031-2035                      | 583                                                                                                                               | 548      | 1,131   | 838                                                                                                              | 761      | 1,599   |
| 2036-2040                      | 308                                                                                                                               | 271      | 579     | 427                                                                                                              | 355      | 782     |
| 2041-2045                      | 137                                                                                                                               | 159      | 296     | 206                                                                                                              | 174      | 380     |
| 2046-2047                      | 168                                                                                                                               | —        | 168     | 181                                                                                                              | —        | 181     |
| Total                          | \$2,575                                                                                                                           | \$ 2,479 | \$5,054 | \$4,476                                                                                                          | \$ 3,993 | \$8,469 |

#### Exposure to the Selected European Countries

The European countries where the Company has exposure and believes heightened uncertainties exist are: Hungary, Italy, Portugal and Spain (collectively, the “Selected European Countries”). 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.

Table of ContentsNet Direct Economic Exposure to Selected European Countries(1)  
As of March 31, 2016

|                           | Hungary<br>(in millions) |         | Italy | Portugal | Spain   | Total |
|---------------------------|--------------------------|---------|-------|----------|---------|-------|
| Sub-sovereign exposure(2) | \$271                    | \$827   | \$ 84 | \$375    | \$1,557 |       |
| Non-sovereign exposure(3) | 179                      | 458     | —     | —        | 637     |       |
| Total                     | \$450                    | \$1,285 | \$ 84 | \$375    | \$2,194 |       |
| Total BIG (See Note 5)    | \$379                    | \$—     | \$ 84 | \$375    | \$838   |       |

(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 and RMBS.

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 \$206 million to Selected European Countries (plus Greece) in transactions with \$4.1 billion of net par outstanding. The indirect exposure to credits with a nexus to Greece is \$6 million across several highly rated pooled corporate obligations with net par outstanding of \$231 million.

## 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 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.

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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 2.88% as of March 31, 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&amp;W

## Roll Forward

|                                                   | First Quarter |         |
|---------------------------------------------------|---------------|---------|
|                                                   | 2016          | 2015    |
|                                                   | (in millions) |         |
| Net expected loss to be paid, beginning of period | \$1,391       | \$1,169 |
| Economic loss development due to:                 |               |         |
| Accretion of discount                             | 9             | 7       |
| Changes in discount rates                         | 63            | 7       |
| Changes in timing and assumptions                 | (13 )         | (17 )   |
| Total economic loss development                   | 59            | (3 )    |
| Paid losses                                       | (113 )        | (12 )   |
| Net expected loss to be paid, end of period       | \$1,337       | \$1,154 |

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

|                                      | Net Expected<br>Loss to be<br>Paid<br>(Recovered)<br>as of<br>December<br>31,<br>2015<br>(2)<br>(in millions) |       | Economic Loss<br>Development | (Paid)<br>Recovered<br>Losses (1) | Net Expected<br>Loss to be<br>Paid<br>(Recovered)<br>as of<br>March 31,<br>2016 (2) |
|--------------------------------------|---------------------------------------------------------------------------------------------------------------|-------|------------------------------|-----------------------------------|-------------------------------------------------------------------------------------|
| Public Finance:                      |                                                                                                               |       |                              |                                   |                                                                                     |
| U.S. public finance                  | \$771                                                                                                         | \$ 98 |                              | \$ (5 )                           | \$ 864                                                                              |
| Non-U.S. public finance              | 38                                                                                                            | 1     |                              | —                                 | 39                                                                                  |
| Public Finance                       | 809                                                                                                           | 99    |                              | (5 )                              | 903                                                                                 |
| Structured Finance:                  |                                                                                                               |       |                              |                                   |                                                                                     |
| U.S. RMBS:                           |                                                                                                               |       |                              |                                   |                                                                                     |
| First lien:                          |                                                                                                               |       |                              |                                   |                                                                                     |
| Prime first lien                     | (2 )                                                                                                          | 0     |                              | 1                                 | (1 )                                                                                |
| Alt-A first lien                     | 127                                                                                                           | (16 ) |                              | (75 )                             | 36                                                                                  |
| Option ARM                           | (28 )                                                                                                         | (21 ) |                              | 2                                 | (47 )                                                                               |
| Subprime                             | 251                                                                                                           | 1     |                              | (12 )                             | 240                                                                                 |
| Total first lien                     | 348                                                                                                           | (36 ) |                              | (84 )                             | 228                                                                                 |
| Second lien                          | 61                                                                                                            | 5     |                              | (1 )                              | 65                                                                                  |
| Total U.S. RMBS                      | 409                                                                                                           | (31 ) |                              | (85 )                             | 293                                                                                 |
| Triple-X life insurance transactions | 99                                                                                                            | 4     |                              | (1 )                              | 102                                                                                 |
| Student loans                        | 54                                                                                                            | (14 ) |                              | (8 )                              | 32                                                                                  |
| Other structured finance             | 20                                                                                                            | 1     |                              | (14 )                             | 7                                                                                   |
| Structured Finance                   | 582                                                                                                           | (40 ) |                              | (108 )                            | 434                                                                                 |
| Total                                | \$1,391                                                                                                       | \$ 59 |                              | \$ (113 )                         | \$ 1,337                                                                            |

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

|                                      | Net Expected<br>Loss to be<br>Paid (Recovered)<br>as of<br>December<br>31,<br>2014<br>(in millions) |         | Economic Loss<br>Development | (Paid)<br>Recovered<br>Losses (1) | Net Expected<br>Loss to be<br>Paid (Recovered)<br>as of<br>March 31, 2015 |
|--------------------------------------|-----------------------------------------------------------------------------------------------------|---------|------------------------------|-----------------------------------|---------------------------------------------------------------------------|
| Public Finance:                      |                                                                                                     |         |                              |                                   |                                                                           |
| U.S. public finance                  | \$ 303                                                                                              | \$ 9    |                              | \$ (2 )                           | \$ 310                                                                    |
| Non-U.S. public finance              | 45                                                                                                  | (3 )    |                              | —                                 | 42                                                                        |
| Public Finance                       | 348                                                                                                 | 6       |                              | (2 )                              | 352                                                                       |
| Structured Finance:                  |                                                                                                     |         |                              |                                   |                                                                           |
| U.S. RMBS:                           |                                                                                                     |         |                              |                                   |                                                                           |
| First lien:                          |                                                                                                     |         |                              |                                   |                                                                           |
| Prime first lien                     | 4                                                                                                   | 0       |                              | (1 )                              | 3                                                                         |
| Alt-A first lien                     | 304                                                                                                 | (5 )    |                              | (10 )                             | 289                                                                       |
| Option ARM                           | (16 )                                                                                               | 4       |                              | (4 )                              | (16 )                                                                     |
| Subprime                             | 303                                                                                                 | (1 )    |                              | (9 )                              | 293                                                                       |
| Total first lien                     | 595                                                                                                 | (2 )    |                              | (24 )                             | 569                                                                       |
| Second lien                          | (11 )                                                                                               | 6       |                              | 6                                 | 1                                                                         |
| Total U.S. RMBS                      | 584                                                                                                 | 4       |                              | (18 )                             | 570                                                                       |
| Triple-X life insurance transactions | 161                                                                                                 | 5       |                              | (1 )                              | 165                                                                       |
| Student loans                        | 68                                                                                                  | (6 )    |                              | —                                 | 62                                                                        |
| Other structured finance             | 8                                                                                                   | (12 )   |                              | 9                                 | 5                                                                         |
| Structured Finance                   | 821                                                                                                 | (9 )    |                              | (10 )                             | 802                                                                       |
| Total                                | \$ 1,169                                                                                            | \$ (3 ) |                              | \$ (12 )                          | \$ 1,154                                                                  |

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 \$2 million and \$4 million in loss adjustment expenses ("LAE") for First Quarter 2016 and 2015, respectively.

(2) Includes expected LAE to be paid of \$9 million as of March 31, 2016 and \$12 million as of December 31, 2015.

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## Future Net R&amp;W Benefit Receivable (Payable)(1)

|             | As of<br>March<br>31,<br>2016 | As of<br>December<br>31, 2015 |
|-------------|-------------------------------|-------------------------------|
|             | (in millions)                 |                               |
| U.S. RMBS:  |                               |                               |
| First lien  | \$ (30 )                      | \$ 0                          |
| Second lien | 77                            | 79                            |
| Total       | \$ 47                         | \$ 79                         |

The Company's agreements with providers of breaches 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. See (1) 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 to pay in claims, 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 March 31, 2016

|                                      | Financial<br>Guaranty<br>Insurance<br>(in millions) | FG VIEs(1)<br>and Other | Credit<br>Derivatives(2) | Total    |
|--------------------------------------|-----------------------------------------------------|-------------------------|--------------------------|----------|
| Public Finance:                      |                                                     |                         |                          |          |
| U.S. public finance                  | \$ 864                                              | \$ —                    | \$ 0                     | \$ 864   |
| Non-U.S. public finance              | 39                                                  | —                       | —                        | 39       |
| Public Finance                       | 903                                                 | —                       | 0                        | 903      |
| Structured Finance:                  |                                                     |                         |                          |          |
| U.S. RMBS:                           |                                                     |                         |                          |          |
| First lien:                          |                                                     |                         |                          |          |
| Prime first lien                     | 2                                                   | —                       | (3 )                     | (1 )     |
| Alt-A first lien                     | 19                                                  | 18                      | (1 )                     | 36       |
| Option ARM                           | (44 )                                               | —                       | (3 )                     | (47 )    |
| Subprime                             | 148                                                 | 55                      | 37                       | 240      |
| Total first lien                     | 125                                                 | 73                      | 30                       | 228      |
| Second lien                          | 19                                                  | 43                      | 3                        | 65       |
| Total U.S. RMBS                      | 144                                                 | 116                     | 33                       | 293      |
| Triple-X life insurance transactions | 91                                                  | —                       | 11                       | 102      |
| Student loans                        | 32                                                  | —                       | —                        | 32       |
| Other structured finance             | 40                                                  | 2                       | (35 )                    | 7        |
| Structured Finance                   | 307                                                 | 118                     | 9                        | 434      |
| Total                                | \$ 1,210                                            | \$ 118                  | \$ 9                     | \$ 1,337 |



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

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

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

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

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

## Net Economic Loss Development (Benefit)

## By Accounting Model

## First Quarter 2016

|                                      | Financial<br>Guaranty<br>Insurance<br>(in millions) | FG<br>and<br>Other | VIEs(1) | Credit<br>Derivatives(2) | Total |
|--------------------------------------|-----------------------------------------------------|--------------------|---------|--------------------------|-------|
| Public Finance:                      |                                                     |                    |         |                          |       |
| U.S. public finance                  | \$98                                                | \$ —               | \$ 0    |                          | \$98  |
| Non-U.S. public finance              | 1                                                   | —                  | 0       |                          | 1     |
| Public Finance                       | 99                                                  | —                  | 0       |                          | 99    |
| Structured Finance:                  |                                                     |                    |         |                          |       |
| U.S. RMBS:                           |                                                     |                    |         |                          |       |
| First lien:                          |                                                     |                    |         |                          |       |
| Prime first lien                     | 0                                                   | —                  | 0       |                          | 0     |
| Alt-A first lien                     | (17 )                                               | 1                  | 0       |                          | (16 ) |
| Option ARM                           | (19 )                                               | —                  | (2 )    |                          | (21 ) |
| Subprime                             | 3                                                   | 0                  | (2 )    |                          | 1     |
| Total first lien                     | (33 )                                               | 1                  | (4 )    |                          | (36 ) |
| Second lien                          | 2                                                   | 3                  | 0       |                          | 5     |
| Total U.S. RMBS                      | (31 )                                               | 4                  | (4 )    |                          | (31 ) |
| Triple-X life insurance transactions | 3                                                   | —                  | 1       |                          | 4     |
| Student loans                        | (14 )                                               | —                  | —       |                          | (14 ) |
| Other structured finance             | 4                                                   | 0                  | (3 )    |                          | 1     |
| Structured Finance                   | (38 )                                               | 4                  | (6 )    |                          | (40 ) |
| Total                                | \$61                                                | \$ 4               | \$ (6 ) |                          | \$59  |



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

|                                      | Financial<br>Guaranty<br>Insurance<br>(in millions) | FG<br>and<br>Other<br>VIEs(1) | Credit<br>Derivatives(2) | Total  |
|--------------------------------------|-----------------------------------------------------|-------------------------------|--------------------------|--------|
| Public Finance:                      |                                                     |                               |                          |        |
| U.S. public finance                  | \$9                                                 | \$ —                          | \$ —                     | \$9    |
| Non-U.S. public finance              | (3 )                                                | —                             | —                        | (3 )   |
| Public Finance                       | 6                                                   | —                             | —                        | 6      |
| Structured Finance:                  |                                                     |                               |                          |        |
| U.S. RMBS:                           |                                                     |                               |                          |        |
| First lien:                          |                                                     |                               |                          |        |
| Prime first lien                     | 1                                                   | —                             | (1 )                     | 0      |
| Alt-A first lien                     | 2                                                   | —                             | (7 )                     | (5 )   |
| Option ARM                           | 1                                                   | —                             | 3                        | 4      |
| Subprime                             | (4 )                                                | 4                             | (1 )                     | (1 )   |
| Total first lien                     | —                                                   | 4                             | (6 )                     | (2 )   |
| Second lien                          | 8                                                   | (1 )                          | (1 )                     | 6      |
| Total U.S. RMBS                      | 8                                                   | 3                             | (7 )                     | 4      |
| Triple-X life insurance transactions | 4                                                   | —                             | 1                        | 5      |
| Student loans                        | (6 )                                                | —                             | —                        | (6 )   |
| Other structured finance             | 0                                                   | (1 )                          | (11 )                    | (12 )  |
| Structured Finance                   | 6                                                   | 2                             | (17 )                    | (9 )   |
| Total                                | \$12                                                | \$ 2                          | \$ (17 )                 | \$(3 ) |

(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 March 31, 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 March 31, 2016, the Company's net exposure 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 \$21 million of net par exposure as of March 31, 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

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failure to 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 \$14.6 billion of net par exposure to healthcare transactions. The BIG net par outstanding in this sector is \$315 million.

The Company projects that its total net expected loss across its troubled U.S. public finance credits as of March 31, 2016, which incorporated the likelihood of the various outcomes, will be \$864 million, compared with a net expected loss of \$771 million as of December 31, 2015. Economic loss development in First Quarter 2016 was \$98 million, 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 gross exposure to these Spanish and Portuguese credits is \$471 million and \$90 million, respectively, and exposure net of reinsurance for Spanish and Portuguese credits is \$375 million and \$84 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 gross exposure to these Hungarian credits is \$274 million and its exposure net of reinsurance is \$271 million, all of which is rated BIG. The Company estimated net expected losses of \$36 million related to these Spanish, Portuguese and Hungarian credits. The economic loss of approximately \$1 million during First Quarter 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.

### First 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 March 31, 2016 as it used as of December 31, 2015, but increased severities for specific vintages of Alt-A first lien and subprime 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

|                                                    | March 31, 2016 | December 31, 2015 |
|----------------------------------------------------|----------------|-------------------|
| Current Loans Modified in the Previous 12 Months   |                |                   |
| Alt A and Prime                                    | 25%            | 25%               |
| Option ARM                                         | 25             | 25                |
| Subprime                                           | 25             | 25                |
| Current Loans Delinquent in the Previous 12 Months |                |                   |
| Alt A and Prime                                    | 25             | 25                |
| Option ARM                                         | 25             | 25                |
| Subprime                                           | 25             | 25                |
| 30 – 59 Days Delinquent                            |                |                   |
| Alt A and Prime                                    | 35             | 35                |
| Option ARM                                         | 40             | 40                |
| Subprime                                           | 45             | 45                |
| 60 – 89 Days Delinquent                            |                |                   |
| Alt A and Prime                                    | 45             | 45                |
| Option ARM                                         | 50             | 50                |
| Subprime                                           | 55             | 55                |
| 90+ Days Delinquent                                |                |                   |
| Alt A and Prime                                    | 55             | 55                |
| Option ARM                                         | 60             | 60                |
| Subprime                                           | 60             | 60                |
| Bankruptcy                                         |                |                   |
| Alt A and Prime                                    | 45             | 45                |
| Option ARM                                         | 50             | 50                |
| Subprime                                           | 40             | 40                |
| Foreclosure                                        |                |                   |
| Alt A and Prime                                    | 65             | 65                |
| Option ARM                                         | 70             | 70                |
| Subprime                                           | 70             | 70                |
| Real Estate Owned                                  |                |                   |
| All                                                | 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 7.5 years after the initial 36-month CDR plateau period, which is the same assumption used at December 31, 2015. 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. 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<br>March 31, 2016 |                  | As of<br>December 31, 2015 |                  |
|---------------------------------------------|-------------------------|------------------|----------------------------|------------------|
|                                             | Range                   | Weighted Average | Range                      | Weighted Average |
| Alt-A First Lien                            |                         |                  |                            |                  |
| Plateau CDR                                 | 0.9% - 27.8%            | 6.4%             | 1.7% - 26.4%               | 6.4%             |
| Intermediate CDR                            | 0.2% - 5.6%             | 1.3%             | 0.3% - 5.3%                | 1.3%             |
| Period until intermediate CDR               | 48 months               |                  | 48 months                  |                  |
| Final CDR                                   | 0.0% - 1.4%             | 0.3%             | 0.1% - 1.3%                | 0.3%             |
| Initial loss severity:                      |                         |                  |                            |                  |
| 2005 and prior                              | 60.0%                   |                  | 60.0%                      |                  |
| 2006                                        | 80.0%                   |                  | 70.0%                      |                  |
| 2007                                        | 65.0%                   |                  | 65.0%                      |                  |
| Initial conditional prepayment rate ("CPR") | 2.7% - 31.6%            | 11.8%            | 2.7% - 32.5%               | 11.5%            |
| Final CPR(2)                                | 15%                     |                  | 15%                        |                  |
| Option ARM                                  |                         |                  |                            |                  |
| Plateau CDR                                 | 3.4% - 10.6%            | 7.8%             | 3.5% - 10.3%               | 7.8%             |
| Intermediate CDR                            | 0.7% - 2.1%             | 1.6%             | 0.7% - 2.1%                | 1.6%             |
| Period until intermediate CDR               | 48 months               |                  | 48 months                  |                  |
| Final CDR                                   | 0.2% - 0.5%             | 0.4%             | 0.2% - 0.5%                | 0.4%             |
| Initial loss severity:                      |                         |                  |                            |                  |
| 2005 and prior                              | 60.0%                   |                  | 60.0%                      |                  |
| 2006                                        | 70.0%                   |                  | 70.0%                      |                  |
| 2007                                        | 65.0%                   |                  | 65.0%                      |                  |
| Initial CPR                                 | 2.0% - 13.7%            | 5.5%             | 1.5% - 10.9%               | 5.1%             |
| Final CPR(2)                                | 15%                     |                  | 15%                        |                  |
| Subprime                                    |                         |                  |                            |                  |
| Plateau CDR                                 | 4.2% - 14.4%            | 9.4%             | 4.7% - 13.2%               | 9.5%             |
| Intermediate CDR                            | 0.8% - 2.9%             | 1.9%             | 0.9% - 2.6%                | 1.9%             |
| Period until intermediate CDR               | 48 months               |                  | 48 months                  |                  |
| Final CDR                                   | 0.2% - 0.7%             | 0.4%             | 0.2% - 0.7%                | 0.4%             |
| Initial loss severity:                      |                         |                  |                            |                  |
| 2005 and prior                              | 80.0%                   |                  | 75.0%                      |                  |
| 2006                                        | 90.0%                   |                  | 90.0%                      |                  |
| 2007                                        | 90.0%                   |                  | 90.0%                      |                  |
| Initial CPR                                 | 0.3% - 9.2%             | 4.2%             | 0.0% - 10.1%               | 3.6%             |
| Final CPR(2)                                | 15%                     |                  | 15%                        |                  |

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

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





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The rate at which the principal amount of loans is voluntarily prepaid may impact both the amount of losses projected (since that amount is a function of the CDR, the loss severity and the loan balance over time) as well as the amount of excess spread (the amount by which the interest paid by the borrowers on the underlying loan exceeds the amount of interest owed on the insured obligations). The assumption for the voluntary CPR follows a similar pattern to that of the CDR. The current level of voluntary prepayments is assumed to continue for the plateau period before gradually increasing over 12 months to the final CPR, which is assumed to be 15% in the base case. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant and the final CPR is not used. These CPR assumptions are the same as those the Company used for 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 March 31, 2016. The Company used a similar approach to establish its pessimistic and optimistic scenarios as of March 31, 2016 as it used as of 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 \$12 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 \$31 million for Alt-A first liens, \$14 million for Option ARM, \$59 million for subprime and \$0.5 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 \$2 million for Alt-A first liens, \$19 million for Option ARM, \$10 million for subprime and \$19 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 \$14 million for Alt-A first liens, \$31 million for Option ARM, \$33 million for subprime and \$0.2 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. Most second lien transactions report the amount of loans in five monthly delinquency categories (i.e., 30-59 days past due, 60-89 days past due, 90-119 days past due, 120-149 days past due and 150-179 days past due). The Company estimates the amount of loans that will default over the next five 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 period that follows the embedded five months of losses. Liquidation rates assumed as of March 31, 2016, were from 25% to 100%.

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

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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 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 December 31, 2015. For March 31, 2016 the Company used the same general approach it had refined in the fourth quarter of 2015 to calculate the number of additional delinquencies as a function of the number of modified loans in the transaction and the final steady state CDR.

When a second lien loan defaults, there is generally a very low recovery. The Company had assumed as of March 31, 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 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 most recent three quarters) 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 December 31, 2015 and March 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 March 31, 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.



Table of ContentsKey Assumptions in Base Case Expected Loss Estimates  
HELOCs (1)

|                           | As of<br>March 31, 2016 |                  |       | As of<br>December 31, 2015 |                  |       |
|---------------------------|-------------------------|------------------|-------|----------------------------|------------------|-------|
|                           | Range                   | Weighted Average |       | Range                      | Weighted Average |       |
| Plateau CDR               | 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%  |
| Period until final CDR    | 34 months               |                  |       | 34 months                  |                  |       |
| Initial CPR               | 11.0%                   | 14.9%            | 11.1% | 10.9%                      |                  |       |
| Final CPR(2)              | 10.0%                   | 15.0%            | 13.3% | 10.0%                      | 15.0%            | 13.3% |
| Loss severity             | 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 \$52 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 \$31 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.

The Company has included in its net expected loss estimates as of March 31, 2016 an estimated net benefit of \$47 million (net of reinsurance). 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 three counterparties where a future reimbursement obligation is collateralized by eligible assets held in trust:

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 March 31, 2016 aggregate lifetime collateral losses on those transactions was \$4.4 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 \$578 million of collateral held in trust for the Company's benefit.

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Deutsche Bank. Under the Company's 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. As of March 31, 2016, the Company was projecting in its base case that such aggregate lifetime claims would remain below \$319 million. In the event aggregate lifetime claims paid exceed \$389 million, Deutsche Bank must reimburse the Company for 85% of such claims paid (in excess of \$389 million) until such claims paid reach \$600 million. Deutsche Bank's reimbursement obligation is secured by \$70 million of collateral held in trust for the Company's benefit.

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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 \$49 million of collateral held in trust for the Company's benefit.

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 \$2.7 billion of net par exposure to Triple-X life insurance transactions as of March 31, 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 March 31, 2016, the Company's projected net expected loss to be paid is \$102 million. The economic loss development during First Quarter 2016 was approximately \$4 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 \$1.8 billion net par of student loan securitizations issued by private issuers and that it classifies as structured finance. Of this amount, \$149 million is rated BIG. The Company is projecting approximately \$32 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 First Quarter 2016 was approximately \$14 million, which was driven primarily by the commutation of certain assumed student loan exposures.

### TruPS and other structured finance

The Company's TruPS sector has BIG par of \$777 million and all other structured finance BIG par totaled \$929 million, comprising primarily transactions backed by perpetual preferred securities, commercial receivables and manufactured housing loans. The Company has expected loss to be paid of \$7 million for TruPS and other structured finance transactions as of March 31, 2016. The economic loss development during First Quarter 2016 was \$1 million, which was attributable primarily to a commercial receivable transaction downgraded to BIG during First Quarter 2016.

### Recovery Litigation

### Public Finance Transactions



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

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On 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 March 31, 2016, \$21 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. The Court's action is subject to appeal.

## 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.

## 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

|                                                  | First<br>Quarter<br>2016 2015<br>(in millions) |       |
|--------------------------------------------------|------------------------------------------------|-------|
| Scheduled net earned premiums                    | \$91                                           | \$96  |
| Acceleration of net earned premiums (1)          | 89                                             | 41    |
| Accretion of discount on net premiums receivable | 3                                              | 4     |
| Financial guaranty insurance net earned premiums | 183                                            | 141   |
| Other                                            | 0                                              | 1     |
| Net earned premiums (2)                          | \$183                                          | \$142 |

(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 \$5 million and \$5 million for First Quarter 2016 and 2015, respectively, related to consolidated FG VIEs.



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## Components of Unearned Premium Reserve

|                          | As of March 31, 2016 |       |         | As of December 31, 2015 |       |         |
|--------------------------|----------------------|-------|---------|-------------------------|-------|---------|
|                          | Gross                | Ceded | Net(1)  | Gross                   | Ceded | Net(1)  |
|                          | (in millions)        |       |         |                         |       |         |
| Deferred premium revenue | 3,829                | 241   | 3,588   | 4,008                   | 238   | 3,770   |
| Contra-paid (2)          | (19 )                | (5 )  | (14 )   | (12 )                   | (6 )  | (6 )    |
| Unearned premium reserve | \$3,810              | \$236 | \$3,574 | \$3,996                 | \$232 | \$3,764 |

(1) Excludes \$105 million and \$110 million of deferred premium revenue, and \$29 million and \$30 million of contra-paid related to FG VIEs as of March 31, 2016 and December 31, 2015, respectively.

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

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

|                                                                 | First Quarter |       |
|-----------------------------------------------------------------|---------------|-------|
|                                                                 | 2016          | 2015  |
|                                                                 | (in millions) |       |
| Beginning of period, December 31                                | \$693         | \$729 |
| Gross premium written, net of commissions on assumed business   | 41            | 36    |
| Gross premiums received, net of commissions on assumed business | (49 )         | (36 ) |
| Adjustments:                                                    |               |       |
| Changes in the expected term                                    | (22 )         | (6 )  |
| Accretion of discount, net of commissions on assumed business   | 0             | 5     |
| Foreign exchange translation                                    | (1 )          | (25 ) |
| Consolidation/deconsolidation of FG VIEs                        | 0             | (4 )  |
| End of period, March 31 (1)                                     | \$662         | \$699 |

(1) Excludes \$16 million and \$22 million as of March 31, 2016 and March 31, 2015, respectively, related to consolidated FG VIEs. Excludes \$1 million related to non-financial guaranty line of business as of March 31, 2015.

Foreign exchange translation relates to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 55%, 52% and 49% of installment premiums at March 31, 2016, December 31, 2015 and March 31, 2015, respectively, are denominated in currencies other than the U.S. dollar, primarily the Euro and British Pound Sterling.

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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 March<br>31, 2016<br>(in millions) |
|--------------------------------|------------------------------------------|
| 2016 (April 1 – June 30)       | \$ 31                                    |
| 2016 (July 1 – September 30)   | 18                                       |
| 2016 (October 1 – December 31) | 17                                       |
| 2017                           | 66                                       |
| 2018                           | 58                                       |
| 2019                           | 55                                       |
| 2020                           | 55                                       |
| 2021-2025                      | 222                                      |
| 2026-2030                      | 147                                      |
| 2031-2035                      | 103                                      |
| After 2035                     | 82                                       |
| Total(1)                       | \$ 854                                   |

(1) Excludes expected cash collections on FG VIEs of \$20 million.

Scheduled Financial Guaranty Insurance Net Earned Premiums

|                                  | As of March<br>31, 2016<br>(in millions) |
|----------------------------------|------------------------------------------|
| 2016 (April 1 – June 30)         | \$ 92                                    |
| 2016 (July 1 – September 30)     | 89                                       |
| 2016 (October 1 – December 31)   | 85                                       |
| 2017                             | 313                                      |
| 2018                             | 290                                      |
| 2019                             | 264                                      |
| 2020                             | 245                                      |
| 2021-2025                        | 955                                      |
| 2026-2030                        | 610                                      |
| 2031-2035                        | 363                                      |
| After 2035                       | 282                                      |
| Net deferred premium revenue(1)  | 3,588                                    |
| Future accretion                 | 179                                      |
| Total future net earned premiums | \$ 3,767                                 |

(1) Excludes scheduled net earned premiums on consolidated FG VIEs of \$105 million.



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Selected Information for Financial Guaranty Insurance  
Policies Paid in Installments

|                                                           | As of<br>March<br>31, 2016 | As of<br>December<br>31, 2015 |
|-----------------------------------------------------------|----------------------------|-------------------------------|
|                                                           | (dollars in millions)      |                               |
| Premiums receivable, net of commission payable            | \$ 662                     | \$ 693                        |
| Gross deferred premium revenue                            | 1,156                      | 1,240                         |
| Weighted-average risk-free rate used to discount premiums | 3.1 %                      | 3.1 %                         |
| Weighted-average period of premiums receivable (in years) | 9.4                        | 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 2.88% as of March 31, 2016 and 0.0% to 3.25% as of December 31, 2015. Financial guaranty insurance expected LAE reserve was \$8 million as of March 31, 2016 and \$10 million as of December 31, 2015.

## Loss and LAE Reserve and Salvage and Subrogation Recoverable

## Net of Reinsurance

## Insurance Contracts

|                                      | As of March 31, 2016 |              |               | As of December 31, 2015 |              |               |
|--------------------------------------|----------------------|--------------|---------------|-------------------------|--------------|---------------|
|                                      | Loss and Salvage and |              |               | Loss and Salvage and    |              |               |
|                                      | LAE                  | Subrogation  | Net Reserve   | LAE                     | Subrogation  | Net Reserve   |
|                                      | Reserve,             | Recoverable, | (Recoverable) | Reserve,                | Recoverable, | (Recoverable) |
|                                      | net                  | net          |               | net                     | net          |               |
|                                      | (in millions)        |              |               |                         |              |               |
| Public Finance:                      |                      |              |               |                         |              |               |
| U.S. public finance                  | \$695                | \$ 7         | \$ 688        | \$604                   | \$ 7         | \$ 597        |
| Non-U.S. public finance              | 27                   | —            | 27            | 25                      | —            | 25            |
| Public Finance                       | 722                  | 7            | 715           | 629                     | 7            | 622           |
| Structured Finance:                  |                      |              |               |                         |              |               |
| U.S. RMBS:                           |                      |              |               |                         |              |               |
| First lien:                          |                      |              |               |                         |              |               |
| Prime first lien                     | 2                    | —            | 2             | 2                       | —            | 2             |
| Alt-A first lien                     | 35                   | 73           | (38 )         | 46                      | —            | 46            |
| Option ARM                           | 10                   | 51           | (41 )         | 13                      | 42           | (29 )         |
| Subprime                             | 161                  | 21           | 140           | 169                     | 21           | 148           |
| First lien                           | 208                  | 145          | 63            | 230                     | 63           | 167           |
| Second lien                          | 34                   | 49           | (15 )         | 32                      | 53           | (21 )         |
| Total U.S. RMBS                      | 242                  | 194          | 48            | 262                     | 116          | 146           |
| Triple-X life insurance transactions | 85                   | —            | 85            | 82                      | —            | 82            |
| Student loans                        | 30                   | —            | 30            | 51                      | —            | 51            |
| Other structured finance             | 32                   | —            | 32            | 48                      | —            | 48            |
| Structured Finance                   | 389                  | 194          | 195           | 443                     | 116          | 327           |
| Subtotal                             | 1,111                | 201          | 910           | 1,072                   | 123          | 949           |
| Other recoverables                   | —                    | 3            | (3 )          | —                       | 3            | (3 )          |
| Subtotal                             | 1,111                | 204          | 907           | 1,072                   | 126          | 946           |
| Effect of consolidating FG VIEs      | (71 )                | —            | (71 )         | (74 )                   | 0            | (74 )         |
| Total (1)                            | \$1,040              | \$ 204       | \$ 836        | \$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<br>March<br>31,<br>2016 | As of<br>December<br>31, 2015 |
|----------------------------------------------------------------|-------------------------------|-------------------------------|
|                                                                | (in millions)                 |                               |
| Loss and LAE reserve                                           | \$1,112                       | \$ 1,067                      |
| Reinsurance recoverable on unpaid losses                       | (72 )                         | (69 )                         |
| Loss and LAE reserve, net                                      | 1,040                         | 998                           |
| Salvage and subrogation recoverable                            | (206 )                        | (126 )                        |
| Salvage and subrogation payable(1)                             | 5                             | 3                             |
| Other recoverables                                             | (3 )                          | (3 )                          |
| Salvage and subrogation recoverable, net and other recoverable | (204 )                        | (126 )                        |
| Net reserves (salvage)                                         | \$836                         | \$ 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: (1) the contra-paid which represent the claim payments made and recoveries received that have not yet been recognized in the statement of operations, (2) 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 (3) 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<br>March 31,<br>2016<br>(in millions) |
|-----------------------------------------------------------------------------------|---------------------------------------------|
| Net expected loss to be paid - financial guaranty insurance (1)                   | \$ 1,210                                    |
| Contra-paid, net                                                                  | 14                                          |
| Salvage and subrogation recoverable, net of reinsurance                           | 201                                         |
| Loss and LAE reserve - financial guaranty insurance contracts, net of reinsurance | (1,038 )                                    |
| Other recoveries                                                                  | 2                                           |
| Net expected loss to be expensed (present value) (2)                              | \$ 389                                      |

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

(2) Excludes \$74 million as of March 31, 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<br>March<br>31, 2016<br>(in<br>millions) |
|------------------------------------|------------------------------------------------|
| 2016 (April 1 – June 30)           | \$ 11                                          |
| 2016 (July 1 – September 30)       | 10                                             |
| 2016 (October 1 – December 31)     | 9                                              |
| Subtotal 2016                      | 30                                             |
| 2017                               | 34                                             |
| 2018                               | 33                                             |
| 2019                               | 30                                             |
| 2020                               | 27                                             |
| 2021-2025                          | 100                                            |
| 2026-2030                          | 70                                             |
| 2031-2035                          | 45                                             |
| After 2035                         | 20                                             |
| Net expected loss to be expensed   | 389                                            |
| Future accretion                   | 156                                            |
| Total expected future loss and LAE | \$ 545                                         |

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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

|                                                                 | First<br>Quarter<br>2016 | 2015<br><br>(in<br>millions) |
|-----------------------------------------------------------------|--------------------------|------------------------------|
| Public Finance:                                                 |                          |                              |
| U.S. public finance                                             | \$97                     | \$13                         |
| Non-U.S. public finance                                         | 0                        | 5                            |
| Public finance                                                  | 97                       | 18                           |
| Structured Finance:                                             |                          |                              |
| U.S. RMBS:                                                      |                          |                              |
| First lien:                                                     |                          |                              |
| Prime first lien                                                | 0                        | 0                            |
| Alt-A first lien                                                | 8                        | (2 )                         |
| Option ARM                                                      | (14 )                    | (1 )                         |
| Subprime                                                        | 4                        | 0                            |
| First lien                                                      | (2 )                     | (3 )                         |
| Second lien                                                     | 13                       | 10                           |
| Total U.S. RMBS                                                 | 11                       | 7                            |
| Triple-X life insurance transactions                            | 3                        | 6                            |
| Student loans                                                   | (14 )                    | (6 )                         |
| Other structured finance                                        | 0                        | (2 )                         |
| Structured finance                                              | 0                        | 5                            |
| Loss and LAE on insurance contracts before FG VIE consolidation | 97                       | 23                           |
| Effect of consolidating FG VIEs                                 | (7 )                     | (5 )                         |
| Loss and LAE                                                    | \$90                     | \$18                         |

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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 March 31, 2016

|                                                       | BIG Categories        |         |         |         |         |         |          |               |          |
|-------------------------------------------------------|-----------------------|---------|---------|---------|---------|---------|----------|---------------|----------|
|                                                       | BIG 1                 |         | BIG 2   |         | BIG 3   |         | Total    | Effect of     | Total    |
|                                                       | Gross                 | Ceded   | Gross   | Ceded   | Gross   | Ceded   | BIG, Net | Consolidating | FG VIEs  |
|                                                       | (dollars in millions) |         |         |         |         |         |          |               |          |
| Number of risks(1)                                    | 202                   | (43 )   | 86      | (14 )   | 129     | (45 )   | 417      | —             | 417      |
| Remaining weighted-average contract period (in years) | 10.1                  | 7.4     | 13.1    | 10.4    | 7.2     | 5.4     | 10.6     | —             | 10.6     |
| Outstanding exposure:                                 |                       |         |         |         |         |         |          |               |          |
| Principal                                             | \$7,084               | \$(499) | \$4,461 | \$(446) | \$3,145 | \$(207) | \$13,538 | \$ —          | \$13,538 |
| Interest                                              | 3,764                 | (214 )  | 3,058   | (233 )  | 962     | (44 )   | 7,293    | —             | 7,293    |
| Total(2)                                              | \$10,848              | \$(713) | \$7,519 | \$(679) | \$4,107 | \$(251) | \$20,831 | \$ —          | \$20,831 |
| Expected cash outflows (inflows)                      | \$337                 | \$(28 ) | \$1,418 | \$(77 ) | \$1,372 | \$(58 ) | \$2,964  | \$ (345 )     | \$2,619  |
| Potential recoveries                                  |                       |         |         |         |         |         |          |               |          |
| Undiscounted R&W                                      | 97                    | (2 )    | (42 )   | 1       | (88 )   | 5       | (29 )    | 6             | (23 )    |
| Other(3)                                              | (590 )                | 16      | (250 )  | 10      | (631 )  | 25      | (1,420 ) | 190           | (1,230 ) |
| Total potential recoveries                            | (493 )                | 14      | (292 )  | 11      | (719 )  | 30      | (1,449 ) | 196           | (1,253 ) |
| Subtotal                                              | (156 )                | (14 )   | 1,126   | (66 )   | 653     | (28 )   | 1,515    | (149 )        | 1,366    |
| Discount                                              | 153                   | (3 )    | (288 )  | 14      | 29      | (94 )   | (189 )   | 33            | (156 )   |
| Present value of expected cash flows                  | \$(3 )                | \$(17 ) | \$838   | \$(52 ) | \$682   | \$(122) | \$1,326  | \$ (116 )     | \$1,210  |
| Deferred premium revenue                              | \$280                 | \$(10 ) | \$156   | \$(7 )  | \$380   | \$(33 ) | \$766    | \$ (96 )      | \$670    |
| Reserves (salvage)                                    | \$(96 )               | \$(12 ) | \$717   | \$(47 ) | \$352   | \$(8 )  | \$906    | \$ (71 )      | \$835    |

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

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

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

(2) Includes BIG amounts related to FG VIEs.

(3) Includes excess spread.

#### Ratings Impact on Financial Guaranty Business

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

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

event with respect to the municipal obligor has occurred, such as the rating of the municipal obligor being downgraded past a specified level, and such condition has been met; (iv) the bank counterparty has elected to terminate the swap; (v) a termination payment is payable by the municipal obligor; and (vi) the municipal obligor has failed to make the termination payment payable by it, then AGM would be required to pay the termination payment due by the municipal obligor, in an amount not to exceed the policy limit set forth in the financial guaranty insurance policy. At AGM's current financial strength ratings, if the conditions giving rise to the obligation of AGM to make a termination payment under the swap termination policies were all satisfied, then AGM could pay claims in an amount not exceeding approximately \$176 million in respect of such termination payments. Taking into consideration whether the



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rating of the municipal obligor is below any applicable specified trigger, if the financial strength ratings of AGM were further downgraded below "A" by S&P or below "A2" by Moody's, and the conditions giving rise to the obligation of AGM to make a payment under the swap policies were all satisfied, then AGM could pay claims in an additional amount not exceeding approximately \$430 million in respect of such termination payments.

As another example, with respect to variable rate demand obligations ("VRDOs") for which a bank has agreed to provide a liquidity facility, a downgrade of AGM or AGC may provide the bank with the right to give notice to bondholders that the bank will terminate the liquidity facility, causing the bondholders to tender their bonds to the bank. Bonds held by the bank accrue interest at a "bank bond rate" that is higher than the rate otherwise borne by the bond (typically the prime rate plus 2.00% — 3.00%, and capped at the lesser of 25% and the maximum legal limit). In the event the bank holds such bonds for longer than a specified period of time, usually 90-180 days, the bank has the right to demand accelerated repayment of bond principal, usually through payment of equal installments over a period of not less than five years. In the event that a municipal obligor is unable to pay interest accruing at the bank bond rate or to pay principal during the shortened amortization period, a claim could be submitted to AGM or AGC under its financial guaranty policy. As of March 31, 2016, AGM and AGC had insured approximately \$5.5 billion net par of VRDOs, of which approximately \$0.3 billion of net par constituted VRDOs issued by municipal obligors rated BBB- or lower pursuant to the Company's internal rating. The specific terms relating to the rating levels that trigger the bank's termination right, and whether it is triggered by a downgrade by one rating agency or a downgrade by all rating agencies then rating the insurer, vary depending on the transaction.

In addition, AGM may be required to pay claims in respect of AGMH's former financial products business if Dexia SA and its affiliates, from which the Company had purchased AGMH and its subsidiaries, do not comply with their obligations following a downgrade of the financial strength rating of AGM. Most of the guaranteed investment contracts ("GICs") insured by AGM allow the GIC holder to terminate the GIC and withdraw the funds in the event of a downgrade of AGM below A3 or A-, with no right of the GIC issuer to avoid such withdrawal by posting collateral or otherwise enhancing its credit. Each GIC contract stipulates the thresholds below which the GIC issuer must post eligible collateral, along with the types of securities eligible for posting and the collateralization percentage applicable to each security type. These collateralization percentages range from 100% of the GIC balance for cash posted as collateral to, typically, 108% for asset-backed securities. If the entire aggregate accreted GIC balance of approximately \$1.7 billion as of March 31, 2016 were terminated, the assets of the GIC issuers (which had an aggregate market value which exceed the liabilities by \$0.8 billion) would be sufficient to fund the withdrawal of the GIC funds.

## 7. Fair Value Measurement

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

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

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

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

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

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

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

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

Level 3—Model derived valuations in which one or more significant inputs or significant value drivers are unobservable. Financial instruments are considered Level 3 when their values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable.

Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation.

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

### Measured and Carried at Fair Value

#### Fixed-Maturity Securities and Short-Term Investments

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

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

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

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

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

- reviews methodologies, any model updates and inputs and compares such information to management's own market information and, where applicable, the internal models,

- reviews internally developed analytic packages that highlight, at a CUSIP level, price changes from the previous quarter to the current quarter, and evaluates, documents, and resolves any significant pricing differences with the assistance of the third party pricing source, and

- compares prices received from different third party pricing sources, and evaluates, documents the rationale for, and resolves any significant pricing differences.

As of March 31, 2016, the Company used models to price 36 fixed-maturity securities (which were purchased or obtained for loss mitigation or other risk management purposes), which were 9.8% or \$1,080 million of the Company's fixed-maturity securities and short-term investments at fair value. Most Level 3 securities were priced with the assistance of an independent third-party. The pricing is based on a discounted cash flow approach using the third-party's proprietary pricing models. The models use inputs such as projected prepayment speeds; severity assumptions; recovery lag assumptions; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); home price depreciation/appreciation rates based on macroeconomic forecasts and recent trading activity. The yield used to discount the projected cash flows is determined by reviewing various attributes of the bond including collateral type, weighted average life, sensitivity to losses, vintage, and convexity, in conjunction with market data on comparable securities. Significant changes to any of these inputs could materially change the expected timing of cash flows within these securities which is a significant factor in determining the fair value of the securities.

### Other Invested Assets

As of March 31, 2016 and December 31, 2015, other invested assets include investments carried and measured at fair value on a recurring basis of \$53 million and \$53 million, respectively, and include primarily an investment in the global property catastrophe risk market and an investment in a fund that invests primarily in senior loans and bonds. Fair values for the majority of these investments are based on their respective net asset value ("NAV") per share or equivalent. Other invested assets also include fixed-maturity securities classified as trading carried as Level 2.

### Other Assets

### Committed Capital Securities

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

### Supplemental Executive Retirement Plans

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

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### Financial Guaranty Contracts Accounted for as Credit Derivatives

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

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

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

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

The fair value of the Company's credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay and the estimated present value of premiums that a financial guarantor of comparable credit-worthiness would hypothetically charge or pay at the reporting date for the same protection. The fair value of the Company's credit derivatives depends on a number of factors, including notional amount of the contract, expected term, credit spreads, changes in interest rates, the credit ratings of referenced entities, the Company's own credit risk and remaining contractual cash flows. The expected remaining contractual premium cash flows are the most readily observable inputs since they are based on the CDS contractual terms. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. Consistent with previous years, market conditions at March 31, 2016 were such that market prices of the Company's CDS contracts were not available.

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

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

#### Assumptions and Inputs

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

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



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

- The weighted average life which is based on Debt Service schedules.

The rates used to discount future expected premium cash flows ranged from 0.44% to 2.06% at March 31, 2016 and 0.44% to 2.51% at December 31, 2015.

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

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

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

- Actual collateral specific credit spreads (if up-to-date and reliable market-based spreads are available).

- Deals priced or closed during a specific quarter within a specific asset class and specific rating. No transactions closed during the periods presented.

- Credit spreads interpolated based upon market indices.

- Credit spreads provided by the counterparty of the CDS.

- Credit spreads extrapolated based upon transactions of similar asset classes, similar ratings, and similar time to maturity.

Information by Credit Spread Type (1)

|                                             | As of<br>March<br>31,<br>2016 |   | As of<br>December<br>31, 2015 |   |
|---------------------------------------------|-------------------------------|---|-------------------------------|---|
| Based on actual collateral specific spreads | 14                            | % | 13                            | % |
| Based on market indices                     | 72                            | % | 73                            | % |
| Provided by the CDS counterparty            | 14                            | % | 14                            | % |
| Total                                       | 100                           | % | 100                           | % |

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(1) Based on par.

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

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

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

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

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

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

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## Example

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

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

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

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

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

## Strengths and Weaknesses of Model

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

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

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

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

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

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

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

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

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

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

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

### Fair Value Option on FG VIEs' Assets and Liabilities

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

The FG VIEs issued securities collateralized by first lien and second lien RMBS as well as loans and receivables. The lowest level input that is significant to the fair value measurement of these assets and liabilities was a Level 3 input (i.e., unobservable), therefore management classified them as Level 3 in the fair value hierarchy. Prices are generally determined with the assistance of an independent third-party, based on a discounted cash flow approach. The models to price the FG VIEs' liabilities used, where appropriate, inputs such as estimated prepayment speeds; market values of the assets that collateralize the securities; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); yields implied by market prices for similar securities; house price depreciation/appreciation rates based on macroeconomic forecasts and, for those liabilities insured by the Company, the benefit from the Company's insurance policy guaranteeing the timely payment of principal and interest, taking into account the timing of the potential default and the Company's own credit rating. The third-party also utilizes an internal model to determine an appropriate yield at which to discount the cash flows of the security, by factoring in collateral types, weighted-average lives, and other structural attributes specific to the security being priced. The expected yield is further calibrated by utilizing algorithms designed to aggregate market color, received by the third-party, on comparable bonds.

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

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

### Not Carried at Fair Value

### Financial Guaranty Insurance Contracts

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



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Long-Term Debt

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

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

Other Invested Assets

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

Other Assets and Other Liabilities

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

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## Financial Instruments Carried at Fair Value

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

## Fair Value Hierarchy of Financial Instruments Carried at Fair Value

As of March 31, 2016

|                                                      | Fair Value Hierarchy |         |         |         |
|------------------------------------------------------|----------------------|---------|---------|---------|
|                                                      | Fair Value Level 1   | Level 2 | Level 3 |         |
|                                                      | (in millions)        |         |         |         |
| Assets:                                              |                      |         |         |         |
| Investment portfolio, available-for-sale:            |                      |         |         |         |
| Fixed-maturity securities                            |                      |         |         |         |
| Obligations of state and political subdivisions      | \$5,776              | \$—     | \$5,769 | \$7     |
| U.S. government and agencies                         | 405                  | —       | 405     | —       |
| Corporate securities                                 | 1,525                | —       | 1,451   | 74      |
| Mortgage-backed securities:                          |                      |         |         |         |
| RMBS                                                 | 1,239                | —       | 879     | 360     |
| CMBS                                                 | 556                  | —       | 556     | —       |
| Asset-backed securities                              | 811                  | —       | 172     | 639     |
| Foreign government securities                        | 276                  | —       | 276     | —       |
| Total fixed-maturity securities                      | 10,588               | —       | 9,508   | 1,080   |
| Short-term investments                               | 459                  | 332     | 127     | —       |
| Other invested assets (1)                            | 12                   | —       | 5       | 7       |
| Credit derivative assets                             | 55                   | —       | —       | 55      |
| FG VIEs' assets, at fair value                       | 1,191                | —       | —       | 1,191   |
| Other assets                                         | 93                   | 26      | 21      | 46      |
| Total assets carried at fair value                   | \$12,398             | \$358   | \$9,661 | \$2,379 |
| Liabilities:                                         |                      |         |         |         |
| Credit derivative liabilities                        | \$489                | \$—     | \$—     | \$489   |
| FG VIEs' liabilities with recourse, at fair value    | 1,165                | —       | —       | 1,165   |
| FG VIEs' liabilities without recourse, at fair value | 119                  | —       | —       | 119     |
| Total liabilities carried at fair value              | \$1,773              | \$—     | \$—     | \$1,773 |

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As of December 31, 2015

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

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

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## Changes in Level 3 Fair Value Measurements

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

### Fair Value Level 3 Rollforward

#### Recurring Basis

#### First Quarter 2016

| Fixed-Maturity Securities                                                                                           |                                                          |                         |       |                                |                           |                                        |                        |                                                         |                                                                     |                                                                     |
|---------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------|-------------------------|-------|--------------------------------|---------------------------|----------------------------------------|------------------------|---------------------------------------------------------|---------------------------------------------------------------------|---------------------------------------------------------------------|
|                                                                                                                     | Obligations<br>of State and<br>Political<br>Subdivisions | Corporate<br>Securities | RMBS  | Asset-<br>Backed<br>Securities | Short-Term<br>Investments | FG VIEs'<br>Assets at<br>Fair<br>Value | Other<br>Assets<br>(8) | Credit<br>Derivative<br>Asset<br>(Liability),<br>net(5) | FG<br>VIEs'<br>Liabilities<br>with<br>Recourse,<br>at Fair<br>Value | FG VIEs'<br>Liabilities<br>without<br>Recourse,<br>at Fair<br>Value |
|                                                                                                                     | (in millions)                                            |                         |       |                                |                           |                                        |                        |                                                         |                                                                     |                                                                     |
| Fair value as of<br>December 31,<br>2015                                                                            | \$8                                                      | \$71                    | \$348 | \$657                          | \$60                      | \$1,261                                | \$65                   | \$(365)                                                 | \$(1,225)                                                           | \$(124)                                                             |
| Total pretax<br>realized and<br>unrealized<br>gains/(losses)<br>recorded in: (1)                                    |                                                          |                         |       |                                |                           |                                        |                        |                                                         |                                                                     |                                                                     |
| Net income (loss)                                                                                                   | 0                                                        | (2)                     | (2)   | (2)                            | 1                         | (2)                                    | (4)                    | (3)                                                     | (16)                                                                | (4)                                                                 |
| Other<br>comprehensive<br>income (loss)                                                                             | 0                                                        | 1                       | (5)   | (5)                            | 0                         | —                                      | 0                      | —                                                       | —                                                                   | —                                                                   |
| Purchases                                                                                                           | —                                                        | —                       | 34    | —                              | —                         | —                                      | —                      | —                                                       | —                                                                   | —                                                                   |
| Settlements                                                                                                         | (1)                                                      | —                       | (15)  | (14)                           | (60)                      | (66)                                   | —                      | (9)                                                     | 39                                                                  | 3                                                                   |
| FG VIE<br>consolidations                                                                                            | —                                                        | —                       | —     | —                              | —                         | —                                      | —                      | —                                                       | —                                                                   | —                                                                   |
| FG VIE<br>deconsolidations                                                                                          | —                                                        | —                       | 0     | —                              | —                         | 0                                      | —                      | —                                                       | 0                                                                   | —                                                                   |
| Fair value as of<br>March 31, 2016                                                                                  | \$7                                                      | \$74                    | \$360 | \$639                          | \$—                       | \$1,191                                | \$49                   | \$(434)                                                 | \$(1,165)                                                           | \$(119)                                                             |
| Change in<br>unrealized<br>gains/(losses)<br>related<br>to financial<br>instruments held<br>as of March 31,<br>2016 | \$0                                                      | \$1                     | \$(6) | \$(5)                          | \$—                       | \$4                                    | \$(16)                 | \$(79)                                                  | \$21                                                                | \$1                                                                 |

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Fair Value Level 3 Rollforward  
Recurring Basis  
First Quarter 2015

|                                                                                                               | Fixed-Maturity Securities                                |                         |       |                                |                                        |                        |                                                         |                                                                  |                                                                     |     |
|---------------------------------------------------------------------------------------------------------------|----------------------------------------------------------|-------------------------|-------|--------------------------------|----------------------------------------|------------------------|---------------------------------------------------------|------------------------------------------------------------------|---------------------------------------------------------------------|-----|
|                                                                                                               | Obligations<br>of State and<br>Political<br>Subdivisions | Corporate<br>Securities | RMBS  | Asset-<br>Backed<br>Securities | FG VIEs'<br>Assets at<br>Fair<br>Value | Other<br>Assets<br>(8) | Credit<br>Derivative<br>Asset<br>(Liability),<br>net(5) | FG VIEs'<br>Liabilities<br>with<br>Recourse,<br>at Fair<br>Value | FG VIEs'<br>Liabilities<br>without<br>Recourse,<br>at Fair<br>Value |     |
|                                                                                                               | (in millions)                                            |                         |       |                                |                                        |                        |                                                         |                                                                  |                                                                     |     |
| Fair value as of<br>December 31, 2014                                                                         | \$38                                                     | \$ 79                   | \$425 | \$ 228                         | \$1,398                                | \$ 37                  | \$ (895 )                                               | \$ (1,277 )                                                      | \$ (142 )                                                           |     |
| Total pretax realized<br>and unrealized<br>gains/(losses)<br>recorded in: (1)                                 |                                                          |                         |       |                                |                                        |                        |                                                         |                                                                  |                                                                     |     |
| Net income (loss)                                                                                             | 3                                                        | (2)                     | 2     | (2)                            | 9                                      | (2)                    | 23                                                      | (3)                                                              | 2                                                                   | (4) |
| Other<br>comprehensive<br>income (loss)                                                                       | (2 )                                                     | (2 )                    | 5     | 1                              | —                                      | 1                      | —                                                       | —                                                                | —                                                                   | —   |
| Purchases                                                                                                     | —                                                        | —                       | 9     | —                              | —                                      | —                      | —                                                       | —                                                                | —                                                                   | —   |
| Settlements                                                                                                   | (31 )                                                    | (7)                     | —     | (65 )                          | (1 )                                   | (30 )                  | —                                                       | (11 )                                                            | 37                                                                  | 2   |
| FG VIE<br>consolidations                                                                                      | —                                                        | —                       | —     | —                              | 104                                    | —                      | —                                                       | (131 )                                                           | —                                                                   | —   |
| FG VIE<br>deconsolidations                                                                                    | —                                                        | —                       | —     | —                              | —                                      | —                      | —                                                       | —                                                                | —                                                                   | —   |
| Fair value as of<br>March 31, 2015                                                                            | \$8                                                      | \$ 79                   | \$383 | \$ 226                         | \$1,495                                | \$ 40                  | \$ (782 )                                               | \$ (1,278 )                                                      | \$ (145 )                                                           |     |
| Change in<br>unrealized<br>gains/(losses) related<br>to financial<br>instruments held as<br>of March 31, 2015 | \$0                                                      | \$ (2 )                 | \$ 7  | \$ 1                           | \$34                                   | \$ 3                   | \$ 103                                                  | \$ (6 )                                                          | \$ (4 )                                                             |     |

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

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

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

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

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

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

(7) Primarily non-cash transaction.

(8) Includes CCS and other invested assets.

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## Level 3 Fair Value Disclosures

## Quantitative Information About Level 3 Fair Value Inputs

At March 31, 2016

| Financial Instrument Description<br>(1)    | Fair Value at<br>March<br>31, 2016<br>(in millions) | Significant Unobservable Inputs                 | Range                  | Weighted Average as<br>a Percentage of<br>Current Par<br>Outstanding |
|--------------------------------------------|-----------------------------------------------------|-------------------------------------------------|------------------------|----------------------------------------------------------------------|
| Assets (2):                                |                                                     |                                                 |                        |                                                                      |
| Fixed-maturity securities (3):             |                                                     |                                                 |                        |                                                                      |
| Corporate securities                       | \$ 74                                               | Yield                                           | 20.2%                  |                                                                      |
|                                            |                                                     | CPR                                             | 1.0 % - 9.8%           | 2.8%                                                                 |
| RMBS                                       | 360                                                 | CDR                                             | 4.8 % - 12.8%          | 9.7%                                                                 |
|                                            |                                                     | Loss severity                                   | 65.0% - 100.0%         | 78.0%                                                                |
|                                            |                                                     | Yield                                           | 3.9 % - 8.9%           | 6.0%                                                                 |
| Asset-backed securities:                   |                                                     |                                                 |                        |                                                                      |
| Investor owned utility                     | 71                                                  | Cash flow receipts                              | 100.0%                 |                                                                      |
|                                            |                                                     | Collateral recovery period                      | 2.7 years              |                                                                      |
|                                            |                                                     | Discount factor                                 | 7.0%                   |                                                                      |
| Triple-X life insurance<br>transactions    | 321                                                 | Yield                                           | 3.5 % - 7.3%           | 4.9%                                                                 |
| Collateralized debt obligations<br>("CDO") | 247                                                 | Yield                                           | 15.0%                  |                                                                      |
|                                            |                                                     | CPR                                             | 2.5 % - 8.6%           | 5.1%                                                                 |
| FG VIEs' assets, at fair value             | 1,191                                               | CDR                                             | 1.2 % - 23.1%          | 5.6%                                                                 |
|                                            |                                                     | Loss severity                                   | 40.0% - 100.0%         | 86.8%                                                                |
|                                            |                                                     | Yield                                           | 3.5 % - 20.9%          | 6.8%                                                                 |
| Other assets                               | 46                                                  | Quotes from third party pricing<br>Term (years) | \$51 - \$54<br>5 years | \$53                                                                 |

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| Financial Instrument Description<br>(1) | Fair Value at<br>March 31,<br>2016<br>(in millions) | Significant Unobservable Inputs | Range         | Weighted Average<br>as a Percentage of<br>Current Par<br>Outstanding |
|-----------------------------------------|-----------------------------------------------------|---------------------------------|---------------|----------------------------------------------------------------------|
| Liabilities:                            |                                                     |                                 |               |                                                                      |
|                                         |                                                     | Year 1 loss estimates           | 0.0 %-41.0%   | 0.8%                                                                 |
|                                         |                                                     | Hedge cost (in bps)             | 25.5 -231.8   | 52.8                                                                 |
| Credit derivative liabilities, net      | (434)                                               | ) Bank profit (in bps)          | 3.8 -1,544.4  | 112.3                                                                |
|                                         |                                                     | Internal floor (in bps)         | 7.0 -100.0    | 18.2                                                                 |
|                                         |                                                     | Internal credit rating          | AAA -CCC      | AA+                                                                  |
|                                         |                                                     | CPR                             | 2.5 %-8.6%    | 5.1%                                                                 |
|                                         |                                                     | CDR                             | 1.2 %-23.1%   | 5.6%                                                                 |
| FG VIEs' liabilities, at fair value     | (1,284)                                             | ) Loss severity                 | 40.0 %-100.0% | 86.8%                                                                |
|                                         |                                                     | Yield                           | 3.5 %-20.9%   | 5.9%                                                                 |

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

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

(3) Excludes obligations of state and political subdivisions investments with fair value of \$7 million.



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## Quantitative Information About Level 3 Fair Value Inputs

At December 31, 2015

| Financial Instrument Description<br>(1) | Fair Value at<br>December<br>31, 2015<br>(in millions) | Significant Unobservable Inputs                 | Range                 | Weighted Average as<br>a Percentage of<br>Current Par<br>Outstanding |
|-----------------------------------------|--------------------------------------------------------|-------------------------------------------------|-----------------------|----------------------------------------------------------------------|
| Assets (2):                             |                                                        |                                                 |                       |                                                                      |
| Fixed-maturity securities (3):          |                                                        |                                                 |                       |                                                                      |
| Corporate securities                    | 71                                                     | Yield                                           | 21.8%                 |                                                                      |
|                                         |                                                        | CPR                                             | 0.3 %-9.0%            | 2.6%                                                                 |
| RMBS                                    | 348                                                    | CDR                                             | 2.7 %-9.3%            | 7.0%                                                                 |
|                                         |                                                        | Loss severity                                   | 60.0 %-100.0%         | 74.0%                                                                |
|                                         |                                                        | Yield                                           | 4.7 %-8.2%            | 6.0%                                                                 |
| Asset-backed securities:                |                                                        |                                                 |                       |                                                                      |
| Investor owned utility                  | 69                                                     | Cash flow receipts                              | 100.0%                |                                                                      |
|                                         |                                                        | Collateral recovery period                      | 2.9 years             |                                                                      |
|                                         |                                                        | Discount factor                                 | 7.0%                  |                                                                      |
| Triple-X life insurance<br>transactions | 329                                                    | Yield                                           | 3.5 %-7.5%            | 5.0%                                                                 |
| CDO                                     | 259                                                    | Yield                                           | 20.0%                 |                                                                      |
| Short-term investments                  | 60                                                     | Yield                                           | 17.0%                 |                                                                      |
|                                         |                                                        | CPR                                             | 0.3 %-9.2%            | 3.9%                                                                 |
| FG VIEs' assets, at fair value          | 1,261                                                  | CDR                                             | 1.2 %-16.0%           | 4.7%                                                                 |
|                                         |                                                        | Loss severity                                   | 40.0 %-100.0%         | 85.9%                                                                |
|                                         |                                                        | Yield                                           | 1.9 %-20.0%           | 6.4%                                                                 |
| Other assets                            | 62                                                     | Quotes from third party pricing<br>Term (years) | \$44 -\$46<br>5 years | \$45                                                                 |

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| Financial Instrument Description<br>(1) | Fair Value at<br>December<br>31, 2015<br>(in millions) | Significant Unobservable Inputs | Range          | Weighted Average<br>as a Percentage of<br>Current Par<br>Outstanding |
|-----------------------------------------|--------------------------------------------------------|---------------------------------|----------------|----------------------------------------------------------------------|
| Liabilities:                            |                                                        |                                 |                |                                                                      |
|                                         | (365)                                                  | Year 1 loss estimates           | 0.0 % -41.0%   | 0.6%                                                                 |
|                                         |                                                        | Hedge cost (in bps)             | 32.8 -282.0    | 66.3                                                                 |
| Credit derivative liabilities, net      |                                                        | Bank profit (in bps)            | 3.8 -1,017.5   | 110.8                                                                |
|                                         |                                                        | Internal floor (in bps)         | 7.0 -100.0     | 16.8                                                                 |
|                                         |                                                        | Internal credit rating          | AAA -CCC       | AA+                                                                  |
|                                         |                                                        | CPR                             | 0.3 % -9.2%    | 3.9%                                                                 |
|                                         |                                                        | CDR                             | 1.2 % -16.0%   | 4.7%                                                                 |
| FG VIEs' liabilities, at fair value     | (1,349)                                                | Loss severity                   | 40.0 % -100.0% | 85.9%                                                                |
|                                         |                                                        | Yield                           | 1.9 % -20.0%   | 5.6%                                                                 |

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

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

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

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

## Fair Value of Financial Instruments

|                                                      | As of<br>March 31, 2016 |                      | As of<br>December 31, 2015 |                      |
|------------------------------------------------------|-------------------------|----------------------|----------------------------|----------------------|
|                                                      | Carrying Amount         | Estimated Fair Value | Carrying Amount            | Estimated Fair Value |
|                                                      | (in millions)           |                      |                            |                      |
| Assets:                                              |                         |                      |                            |                      |
| Fixed-maturity securities                            | \$10,588                | \$10,588             | \$10,627                   | \$10,627             |
| Short-term investments                               | 459                     | 459                  | 396                        | 396                  |
| Other invested assets (1)                            | 150                     | 152                  | 150                        | 152                  |
| Credit derivative assets                             | 55                      | 55                   | 81                         | 81                   |
| FG VIEs' assets, at fair value                       | 1,191                   | 1,191                | 1,261                      | 1,261                |
| Other assets                                         | 211                     | 211                  | 206                        | 206                  |
| Liabilities:                                         |                         |                      |                            |                      |
| Financial guaranty insurance contracts (2)           | 3,804                   | 9,500                | 3,998                      | 8,712                |
| Long-term debt                                       | 1,302                   | 1,500                | 1,300                      | 1,512                |
| Credit derivative liabilities                        | 489                     | 489                  | 446                        | 446                  |
| FG VIEs' liabilities with recourse, at fair value    | 1,165                   | 1,165                | 1,225                      | 1,225                |
| FG VIEs' liabilities without recourse, at fair value | 119                     | 119                  | 124                        | 124                  |
| Other liabilities                                    | 73                      | 73                   | 9                          | 9                    |

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

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

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8. Financial Guaranty Contracts Accounted for as Credit Derivatives

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

Credit derivative transactions are governed by ISDA documentation and have different characteristics from financial guaranty insurance contracts. For example, the Company's control rights with respect to a reference obligation under a credit derivative may be more limited than when the Company issues a financial guaranty insurance contract. In addition, there are more circumstances under which the Company may be obligated to make payments. Similar to a financial guaranty insurance contract, the Company would be obligated to pay if the obligor failed to make a scheduled payment of principal or interest in full. However, the Company may also be required to pay if the obligor becomes bankrupt or if the reference obligation were restructured if, after negotiation, those credit events are specified in the documentation for the credit derivative transactions. Furthermore, the Company may be required to make a payment due to an event that is unrelated to the performance of the obligation referenced in the credit derivative. If events of default or termination events specified in the credit derivative documentation were to occur, the non-defaulting or the non-affected party, which may be either the Company or the counterparty, depending upon the circumstances, may decide to terminate a credit derivative prior to maturity. In that case, the Company may be required to make a termination payment to its swap counterparty upon such termination. The Company may not unilaterally terminate a CDS contract; however, the Company on occasion has mutually agreed with various counterparties to terminate certain CDS transactions.

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## Credit Derivative Net Par Outstanding by Sector

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

Credit Derivatives  
Subordination and Ratings

| Asset Type                                                 | As of March 31, 2016  |               |               |          |        | As of December 31, 2015 |               |               |          |        |
|------------------------------------------------------------|-----------------------|---------------|---------------|----------|--------|-------------------------|---------------|---------------|----------|--------|
|                                                            | Net Par               | Original      | Current       | Weighted |        | Net Par                 | Original      | Current       | Weighted |        |
|                                                            | Outstanding           | Subordination | Subordination | Credit   | Rating | Outstanding             | Subordination | Subordination | Credit   | Rating |
|                                                            | (dollars in millions) |               |               |          |        |                         |               |               |          |        |
| Pooled corporate obligations:                              |                       |               |               |          |        |                         |               |               |          |        |
| Collateralized loan obligation/collateral bond obligations | \$5,197               | 30.7 %        | 42.8 %        | AAA      |        | \$5,873                 | 30.9 %        | 42.3 %        | AAA      |        |
| Synthetic investment grade pooled corporate                | 7,127                 | 21.7          | 19.4          | AAA      |        | 7,108                   | 21.7          | 19.4          | AAA      |        |
| TruPS CDOs                                                 | 3,394                 | 45.6          | 42.9          | A-       |        | 3,429                   | 45.8          | 42.6          | A-       |        |
| Market value CDOs of corporate obligations                 | 1,113                 | 17.0          | 27.8          | AAA      |        | 1,113                   | 17.0          | 30.1          | AAA      |        |
| Total pooled corporate obligations                         | 16,831                | 29.0          | 31.9          | AAA      |        | 17,523                  | 29.2          | 32.3          | AAA      |        |
| U.S. RMBS:                                                 |                       |               |               |          |        |                         |               |               |          |        |
| Option ARM and Alt-A first lien                            | 336                   | 10.5          | 12.8          | AA-      |        | 351                     | 10.5          | 12.7          | AA-      |        |
| Subprime first lien                                        | 951                   | 27.7          | 45.0          | AA       |        | 981                     | 27.7          | 45.2          | AA       |        |
| Prime first lien                                           | 169                   | 10.9          | 0.0           | BB       |        | 177                     | 10.9          | 0.0           | BB       |        |
| Closed-end second lien                                     | 16                    | —             | —             | CCC      |        | 17                      | —             | —             | CCC      |        |
| Total U.S. RMBS                                            | 1,472                 | 24.1          | 37.3          | A+       |        | 1,526                   | 24.1          | 37.4          | A+       |        |
| CMBS                                                       | 496                   | 44.7          | 53.8          | AAA      |        | 530                     | 44.8          | 52.6          | AAA      |        |
| Other                                                      | 6,067                 | —             | —             | A        |        | 6,015                   | —             | —             | A        |        |
| Total                                                      | \$24,866              |               |               | AA+      |        | \$25,594                |               |               | AA+      |        |

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

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

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

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

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The Company's exposure to "Other" CDS contracts is also highly diversified. It includes \$1.8 billion of exposure to one pooled infrastructure transaction comprising diversified pools of international infrastructure project transactions and loans to regulated utilities. These pools were all structured with underlying credit enhancement sufficient for the Company to attach at AAA levels at origination. The remaining \$4.3 billion of exposure in "Other" CDS contracts comprises numerous deals across various asset classes, such as commercial receivables, international RMBS, infrastructure, regulated utilities and consumer receivables.

## Distribution of Credit Derivative Net Par Outstanding by Internal Rating

| Ratings                               | As of March 31,<br>2016                         |            |   | As of December 31,<br>2015 |            |   |
|---------------------------------------|-------------------------------------------------|------------|---|----------------------------|------------|---|
|                                       | Net Par<br>Outstanding<br>(dollars in millions) | % of Total |   | Net Par<br>Outstanding     | % of Total |   |
| AAA                                   | \$14,302                                        | 57.5       | % | \$14,808                   | 57.9       | % |
| AA                                    | 4,624                                           | 18.6       |   | 4,821                      | 18.8       |   |
| A                                     | 2,253                                           | 9.1        |   | 2,144                      | 8.4        |   |
| BBB                                   | 2,108                                           | 8.5        |   | 2,212                      | 8.6        |   |
| BIG                                   | 1,579                                           | 6.3        |   | 1,609                      | 6.3        |   |
| Credit derivative net par outstanding | \$24,866                                        | 100.0      | % | \$25,594                   | 100.0      | % |

## Fair Value of Credit Derivatives

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

|                                                                                                 | First Quarter<br>2016 2015<br>(in millions) |       |
|-------------------------------------------------------------------------------------------------|---------------------------------------------|-------|
| Realized gains on credit derivatives                                                            | \$10                                        | \$23  |
| Net credit derivative losses (paid and payable) recovered and recoverable and other settlements | (2 )                                        | (2 )  |
| Realized gains (losses) and other settlements on credit derivatives                             | 8                                           | 21    |
| Net change in unrealized gains (losses) on credit derivatives:                                  |                                             |       |
| Pooled corporate obligations                                                                    | (48 )                                       | 17    |
| U.S. RMBS                                                                                       | (15 )                                       | 75    |
| CMBS                                                                                            | 0                                           | 0     |
| Other                                                                                           | (5 )                                        | 11    |
| Net change in unrealized gains (losses) on credit derivatives                                   | (68 )                                       | 103   |
| Net change in fair value of credit derivatives                                                  | \$(60)                                      | \$124 |

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

First  
Quarter  
2016  
(in  
millions)

|                                                   |           |
|---------------------------------------------------|-----------|
| Net par of terminated credit derivative contracts | \$ —\$ 93 |
| Realized gains on credit derivatives              | 0 11      |



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During First Quarter 2016, unrealized fair value losses were generated primarily in the trust preferred, and U.S. RMBS prime first lien and subprime sectors, due to wider implied net spreads. The wider implied net spreads were primarily a result of the decreased cost to buy protection on AGC and AGM, particularly for the one year and five year CDS spreads. These transactions were pricing at or above their floor levels (or the minimum rate at which the Company would consider assuming these risks based on historical experience); therefore when the cost of purchasing CDS protection on AGC and AGM, which management refers to as the CDS spread on AGC and AGM, decreased the implied spreads that the Company would expect to receive on these transactions increased. Unrealized fair value losses in the Other Sector were generated primarily by a price decline on a hedge the Company has against another financial guarantor. These losses were partially offset by an unrealized fair value gain on a terminated toll road securitization.

During First Quarter 2015, unrealized fair value gains were generated primarily in the U.S. RMBS prime first lien and Option ARM sectors. The change in fair value of credit derivatives in First Quarter 2015 was primarily due to a refinement in methodology to address an instance in a U.S. RMBS transaction that changed from an expected loss to an expected recovery position. This refinement resulted in approximately \$49 million in fair value gains in First Quarter 2015. In addition, there were unrealized gains in the TruPS CDO and Other sectors as result of price improvements on the underlying collateral. The changes in the Company's CDS spreads did not have a material impact during the quarter.

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

**CDS Spread on AGC and AGM**

Quoted price of CDS contract (in basis points)

|                       | As of<br>March<br>31,<br>2016 | As of<br>December<br>31, 2015 | As of<br>March<br>31,<br>2015 | As of<br>December<br>31, 2014 |
|-----------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| Five-year CDS spread: |                               |                               |                               |                               |
| AGC                   | 307                           | 376                           | 317                           | 323                           |
| AGM                   | 309                           | 366                           | 341                           | 325                           |
| One-year CDS spread   |                               |                               |                               |                               |
| AGC                   | 105                           | 139                           | 60                            | 80                            |
| AGM                   | 102                           | 131                           | 80                            | 85                            |

**Fair Value of Credit Derivatives Assets (Liabilities)**

and Effect of AGC and AGM

Credit Spreads

As of      As of  
March      December  
31, 2016   31, 2015  
(in millions)

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|                                                                              |           |             |
|------------------------------------------------------------------------------|-----------|-------------|
| Fair value of credit derivatives before effect of AGC and AGM credit spreads | \$(1,509) | \$ (1,448 ) |
| Plus: Effect of AGC and AGM credit spreads                                   | 1,075     | 1,083       |
| Net fair value of credit derivatives (1)                                     | \$(434 )  | \$ (365 )   |

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

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

The following table presents the fair value and the present value of expected claim payments or recoveries (i.e. net expected loss to be paid as described in Note 6) for contracts accounted for as derivatives.

Net Fair Value and Expected Losses  
of Credit Derivatives by Sector

| Asset Type                   | Fair Value of Credit<br>Asset (Liability), net |                               | Expected Loss to<br>Derivative<br>be (Paid)<br>Recovered |                               |
|------------------------------|------------------------------------------------|-------------------------------|----------------------------------------------------------|-------------------------------|
|                              | As of<br>March<br>31,<br>2016                  | As of<br>December<br>31, 2015 | As<br>of<br>March<br>31,<br>2016                         | As of<br>December<br>31, 2015 |
|                              | (in millions)                                  |                               |                                                          |                               |
| Pooled corporate obligations | \$(131 )                                       | \$(82 )                       | \$(4 )                                                   | \$(5 )                        |
| U.S. RMBS                    | (113 )                                         | (98 )                         | (33 )                                                    | (38 )                         |
| CMBS                         | 0                                              | 0                             | —                                                        | —                             |
| Other                        | (190 )                                         | (185 )                        | 28                                                       | 27                            |
| Total                        | \$(434 )                                       | \$(365 )                      | \$(9 )                                                   | \$(16 )                       |

Ratings Sensitivities of Credit Derivative Contracts

Within the Company's insured CDS portfolio, the transaction documentation for approximately \$3.7 billion in CDS gross par insured as of March 31, 2016 requires AGC to post eligible collateral to secure its obligations to make payments under such contracts. Eligible collateral is generally cash or U.S. government or agency securities; eligible collateral other than cash is valued at a discount to the face amount.

For approximately \$3.5 billion of such contracts, AGC has negotiated caps such that the posting requirement cannot exceed a certain fixed amount, regardless of the mark-to-market valuation of the exposure or the financial strength ratings of AGC. For such contracts, AGC need not post on a cash basis an aggregate of more than \$575 million, although the value of the collateral posted may exceed such fixed amount depending on the advance rate agreed with the counterparty for the particular type of collateral posted.

For the remaining approximately \$219 million of such contracts, AGC could be required from time to time to post additional collateral without such cap based on movements in the mark-to-market valuation of the underlying exposure.

As of March 31, 2016, the Company was posting approximately \$308 million to secure its obligations under CDS, of which approximately \$23 million related to the \$219 million of notional described above, as to which the obligation to collateralize is not capped. In contrast, as of December 31, 2015, the Company was posting approximately \$305

million to secure its obligations under CDS, of which approximately \$23 million related to \$221 million of notional as to which the obligation to collateralize was not capped. The obligation to post collateral could impair the Company's liquidity and results of operations.

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## Sensitivity to Changes in Credit Spread

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

## Effect of Changes in Credit Spread

As of March 31, 2016

| Credit Spreads(1)        | Estimated Change<br>in Fair Value<br>(Pre-Tax)<br>(in millions) | Estimated Change<br>in Fair Value<br>(Pre-Tax)<br>(in millions) |
|--------------------------|-----------------------------------------------------------------|-----------------------------------------------------------------|
| 100% widening in spreads | \$(883)                                                         | \$ (449)                                                        |
| 50% widening in spreads  | (658)                                                           | (224)                                                           |
| 25% widening in spreads  | (547)                                                           | (113)                                                           |
| 10% widening in spreads  | (479)                                                           | (45)                                                            |
| Base Scenario            | (434)                                                           | —                                                               |
| 10% narrowing in spreads | (392)                                                           | 42                                                              |
| 25% narrowing in spreads | (329)                                                           | 105                                                             |
| 50% narrowing in spreads | (226)                                                           | 208                                                             |

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

## 9. Consolidated Variable Interest Entities

## Consolidated FG VIEs

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

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

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

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

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

## Number of FG VIEs Consolidated

|                                      | First<br>Quarter<br>2016 2015 |    |
|--------------------------------------|-------------------------------|----|
| Beginning of the period, December 31 | 34                            | 32 |
| Consolidated (1)                     | —                             | 1  |
| Deconsolidated (1)                   | (1 )                          | —  |
| End of the period, September 30      | 33                            | 33 |

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

The total unpaid principal balance for the FG VIEs’ assets that were over 90 days or more past due was approximately \$146 million at March 31, 2016 and \$154 million at December 31, 2015. The aggregate unpaid principal of the FG VIEs’ assets was approximately \$776 million greater than the aggregate fair value at March 31, 2016, excluding the effect of R&W settlements. The aggregate unpaid principal of the FG VIEs’ assets was approximately \$804 million greater than the aggregate fair value at December 31, 2015, excluding the effect of R&W settlements.

The change in the instrument-specific credit risk of the FG VIEs’ assets held as of March 31, 2016 that was recorded in the consolidated statements of operations for First Quarter 2016 were gains of \$34 million. The change in the instrument-specific credit risk of the FG VIEs’ assets held as of March 31, 2015 that was recorded in the consolidated statements of operations for First Quarter 2015 were gains of \$18 million. To calculate the instrument specific credit risk, the changes in the fair value of the FG VIE assets are allocated between changes that are due to the instrument specific credit risk and changes due to other factors, including interest rates. The instrument specific credit risk amount is determined by using expected contractual cash flows versus current expected cash flows discounted at original contractual rate. The net present value is calculated by discounting the expected cash flows of the underlying security, excluding the Company’s financial guaranty insurance, at the relevant effective interest rate.

The unpaid principal for FG VIE liabilities with recourse, which represent obligations insured by AGC or AGM, was \$1,382 million and \$1,436 million as of March 31, 2016 and December 31, 2015, respectively. FG VIE liabilities with recourse will mature at various dates ranging from 2025 to 2038. The aggregate unpaid principal balance of the FG VIE liabilities with and without recourse was approximately \$407 million greater than the aggregate fair value of the FG VIEs’ liabilities as of March 31, 2016. The aggregate unpaid principal balance was approximately \$423 million greater than the aggregate fair value of the FG VIEs’ liabilities as of December 31, 2015.





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

## Consolidated FG VIEs

## By Type of Collateral

|                       | As of March 31,<br>2016 |             | As of December<br>31, 2015 |             |
|-----------------------|-------------------------|-------------|----------------------------|-------------|
|                       | Assets                  | Liabilities | Assets                     | Liabilities |
|                       | (in millions)           |             |                            |             |
| With recourse:        |                         |             |                            |             |
| U.S. RMBS first lien  | \$457                   | \$ 495      | \$506                      | \$ 521      |
| U.S. RMBS second lien | 189                     | 250         | 194                        | 273         |
| Life insurance        | 339                     | 339         | 347                        | 347         |
| Manufactured housing  | 81                      | 81          | 84                         | 84          |
| Total with recourse   | 1,066                   | 1,165       | 1,131                      | 1,225       |
| Without recourse      | 125                     | 119         | 130                        | 124         |
| Total                 | \$1,191                 | \$ 1,284    | \$1,261                    | \$ 1,349    |

The consolidation of FG VIEs has a significant effect on net income and shareholders' equity due to (1) changes in fair value gains (losses) on FG VIE assets and liabilities, (2) the elimination of premiums and losses related to the AGC and AGM FG VIE liabilities with recourse and (3) the elimination of investment balances related to the Company's purchase of AGC and AGM insured FG VIE debt. Upon consolidation of a FG VIE, the related insurance and, if applicable, the related investment balances, are considered intercompany transactions and therefore eliminated. Such eliminations are included in the table below to present the full effect of consolidating FG VIEs.

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

|                                                | First<br>Quarter<br>2016 2015<br>(in millions) |         |
|------------------------------------------------|------------------------------------------------|---------|
| Net earned premiums                            | \$ (5 )                                        | \$ (5 ) |
| Net investment income                          | (5 )                                           | (3 )    |
| Net realized investment gains (losses)         | 1                                              | 0       |
| Fair value gains (losses) on FG VIEs           | 18                                             | (7 )    |
| Loss and LAE                                   | 6                                              | 5       |
| Effect on income before tax                    | 15                                             | (10 )   |
| Less: tax provision (benefit)                  | 5                                              | (4 )    |
| Effect on net income (loss)                    | \$ 10                                          | \$ (6 ) |
| Effect on cash flows from operating activities | \$ 6                                           | \$ 18   |

As of As of  
March December  
31, 31, 2015

2016

(in millions)

Effect on shareholders' equity (decrease) increase \$(12) \$ (23 )

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Fair value gains (losses) on FG VIEs represent the net change in fair value on the consolidated FG VIEs' assets and liabilities. During First Quarter 2016, the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of \$18 million. The primary driver of the gain was price appreciation on the FG VIE assets during the quarter resulting from improvements in the underlying collateral.

During First Quarter 2015, the Company recorded a pre-tax net fair value loss on consolidated FG VIEs of \$7 million. The primary driver of the loss was a pre-tax net fair value loss of \$26 million on the consolidation of one new FG VIE. The net fair value loss on consolidation was partially offset by price appreciation on the FG VIE assets during the quarter resulting from improvements in the underlying collateral.

## Other Consolidated VIEs

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

## Non-Consolidated VIEs

As of March 31, 2016 and December 31, 2015, the Company had financial guaranty contracts outstanding for approximately 720 and 750 VIEs, respectively, that it did not consolidate. To date, the Company's analyses have indicated that it does not have a controlling financial interest in any other VIEs and, as a result, they are not consolidated. The Company's exposure provided through its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 4, Outstanding Exposure.

## 10. Investments and Cash

## Net Investment Income and Realized Gains (Losses)

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. Accrued investment income, which is recorded in Other Assets, was \$98 million and \$99 million as of March 31, 2016 and December 31, 2015, respectively.

## Net Investment Income

|                                                                | First<br>Quarter<br>2016 2015<br>(in millions) |       |
|----------------------------------------------------------------|------------------------------------------------|-------|
| Income from fixed-maturity securities managed by third parties | \$79                                           | \$82  |
| Income from internally managed securities:                     |                                                |       |
| Fixed maturities                                               | 17                                             | 15    |
| Other                                                          | 5                                              | 6     |
| Gross investment income                                        | 101                                            | 103   |
| Investment expenses                                            | (2 )                                           | (2 )  |
| Net investment income                                          | \$99                                           | \$101 |



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## Net Realized Investment Gains (Losses)

|                                                               | First<br>Quarter<br>2016 | 2015 |
|---------------------------------------------------------------|--------------------------|------|
|                                                               | (in<br>millions)         |      |
| Gross realized gains on available-for-sale securities         | \$6                      | \$24 |
| Gross realized gains on other assets in investment portfolio  | —                        | 1    |
| Gross realized losses on available-for-sale securities        | (2 )                     | (1 ) |
| Gross realized losses on other assets in investment portfolio | (1 )                     | (1 ) |
| Other-than-temporary impairment                               | (16 )                    | (7 ) |
| Net realized investment gains (losses)                        | \$(13)                   | \$16 |

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

Roll Forward of Credit Losses  
in the Investment Portfolio

|                                                                                                                      | First Quarter<br>2016 | 2015  |
|----------------------------------------------------------------------------------------------------------------------|-----------------------|-------|
|                                                                                                                      | (in millions)         |       |
| Balance, beginning of period                                                                                         | \$108                 | \$124 |
| Additions for credit losses on securities for which an other-than-temporary-impairment was not previously recognized | 1                     | —     |
| Reductions for securities sold and other settlement during the period                                                | (2 )                  | (21 ) |
| Additions for credit losses on securities for which an other-than-temporary-impairment was previously recognized     | 0                     | 3     |
| Balance, end of period                                                                                               | \$107                 | \$106 |

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## Investment Portfolio

## Fixed-Maturity Securities and Short-Term Investments

## by Security Type

As of March 31, 2016

| Investment Category                             | Percent<br>of<br>Total(1) | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair<br>Value | AOCI(2)<br>Gain<br>(Loss) on<br>Securities<br>with<br>Other-Than-Temporary<br>Impairment | Weighted<br>Average<br>Credit<br>Rating<br>(3) |
|-------------------------------------------------|---------------------------|-------------------|------------------------------|-------------------------------|----------------------------|------------------------------------------------------------------------------------------|------------------------------------------------|
| (dollars in millions)                           |                           |                   |                              |                               |                            |                                                                                          |                                                |
| Fixed-maturity securities:                      |                           |                   |                              |                               |                            |                                                                                          |                                                |
| Obligations of state and political subdivisions | 51 %                      | \$ 5,417          | \$ 360                       | \$ (1 )                       | \$ 5,776                   | \$ 3                                                                                     | AA                                             |
| U.S. government and agencies                    | 4                         | 379               | 26                           | 0                             | 405                        | —                                                                                        | AA+                                            |
| Corporate securities                            | 14                        | 1,473             | 69                           | (17 )                         | 1,525                      | (11 )                                                                                    | A-                                             |
| Mortgage-backed securities(4):                  | 0                         |                   |                              |                               |                            |                                                                                          |                                                |
| RMBS                                            | 11                        | 1,222             | 37                           | (20 )                         | 1,239                      | (13 )                                                                                    | A                                              |
| CMBS                                            | 5                         | 531               | 25                           | 0                             | 556                        | —                                                                                        | AAA                                            |
| Asset-backed securities                         | 8                         | 821               | 3                            | (13 )                         | 811                        | (11 )                                                                                    | B+                                             |
| Foreign government securities                   | 3                         | 280               | 5                            | (9 )                          | 276                        | —                                                                                        | AA+                                            |
| Total fixed-maturity securities                 | 96                        | 10,123            | 525                          | (60 )                         | 10,588                     | (32 )                                                                                    | A+                                             |
| Short-term investments                          | 4                         | 459               | 0                            | 0                             | 459                        | —                                                                                        | AAA                                            |
| Total investment portfolio                      | 100 %                     | \$ 10,582         | \$ 525                       | \$ (60 )                      | \$ 11,047                  | \$ (32 )                                                                                 | A+                                             |

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

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

(1) Based on amortized cost.

(2) Accumulated OCI. See also Note 17, Shareholders' Equity.

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

(4) Government-agency obligations were approximately 52% of mortgage backed securities as of March 31, 2016 and 54% as of December 31, 2015 based on fair value.

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

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

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

## Fixed-Maturity Securities

## Gross Unrealized Loss by Length of Time

As of March 31, 2016

|                                                           | Less than 12 months   |                 | 12 months or more |                 | Total      |                 |
|-----------------------------------------------------------|-----------------------|-----------------|-------------------|-----------------|------------|-----------------|
|                                                           | Fair Value            | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |
|                                                           | (dollars in millions) |                 |                   |                 |            |                 |
| Obligations of state and political subdivisions           | \$58                  | \$ 0            | \$ 87             | \$ (1           | \$145      | \$ (1           |
| U.S. government and agencies                              | 7                     | 0               | —                 | —               | 7          | 0               |
| Corporate securities                                      | 78                    | (2              | 122               | (15             | 200        | (17             |
| Mortgage-backed securities:                               |                       |                 |                   |                 |            |                 |
| RMBS                                                      | 123                   | (5              | 182               | (15             | 305        | (20             |
| CMBS                                                      | 7                     | 0               | 5                 | 0               | 12         | 0               |
| Asset-backed securities                                   | 456                   | (13             | —                 | —               | 456        | (13             |
| Foreign government securities                             | 91                    | (4              | 53                | (5              | 144        | (9              |
| Total                                                     | \$820                 | \$ (24          | \$ 449            | \$ (36          | \$1,269    | \$ (60          |
| Number of securities (1)                                  |                       | 110             |                   | 82              |            | 185             |
| Number of securities with other-than-temporary impairment |                       | 12              |                   | 6               |            | 18              |



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## Fixed-Maturity Securities

## Gross Unrealized Loss by Length of Time

As of December 31, 2015

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

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

Of the securities in an unrealized loss position for 12 months or more as of March 31, 2016, eleven securities had unrealized losses greater than 10% of book value. The total unrealized loss for these securities as of March 31, 2016 was \$26 million. The Company has determined that the unrealized losses recorded as of March 31, 2016 are yield related and not the result of other-than-temporary-impairment.

The amortized cost and estimated fair value of available-for-sale fixed maturity securities by contractual maturity as of March 31, 2016 are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

## Distribution of Fixed-Maturity Securities

## by Contractual Maturity

As of March 31, 2016

|                                       | Amortized Cost | Estimated Fair Value |
|---------------------------------------|----------------|----------------------|
|                                       | (in millions)  |                      |
| Due within one year                   | \$469          | \$ 470               |
| Due after one year through five years | 1,654          | 1,719                |
| Due after five years through 10 years | 2,195          | 2,320                |
| Due after 10 years                    | 4,052          | 4,284                |
| Mortgage-backed securities:           |                |                      |
| RMBS                                  | 1,222          | 1,239                |
| CMBS                                  | 531            | 556                  |
| Total                                 | \$10,123       | \$ 10,588            |



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The investment portfolio contains securities and cash that are either held in trust for the benefit of third party reinsurers in accordance with statutory requirements, invested in a guaranteed investment contract for future claims payments, placed on deposit to fulfill state licensing requirements, or otherwise restricted in the amount of \$300 million and \$283 million as of March 31, 2016 and December 31, 2015, respectively, based on fair value. The investment portfolio also contains securities that are held in trust by certain AGL subsidiaries for the benefit of other AGL subsidiaries in accordance with statutory and regulatory requirements in the amount of \$1,550 million and \$1,411 million as of March 31, 2016 and December 31, 2015, respectively, based on fair value.

The fair value of the Company's pledged securities to secure its obligations under its CDS exposure totaled \$308 million and \$305 million as of March 31, 2016 and December 31, 2015, respectively.

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

**Internally Managed Portfolio**

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

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

**Internally Managed Portfolio  
Carrying Value**

|                                                                          | As of<br>March<br>31,<br>2016 | As of<br>December<br>31, 2015 |
|--------------------------------------------------------------------------|-------------------------------|-------------------------------|
|                                                                          | (in millions)                 |                               |
| Assets purchased for loss mitigation and other risk management purposes: |                               |                               |
| Fixed-maturity securities, at fair value                                 | \$1,264                       | \$ 1,266                      |
| Other invested assets                                                    | 112                           | 114                           |
| Other                                                                    | 55                            | 55                            |
| Total                                                                    | \$1,431                       | \$ 1,435                      |

**11. Insurance Company Regulatory Requirements****Dividend Restrictions and Capital Requirements**

Under New York insurance law, AGM may only pay dividends out of "earned surplus," which is the portion of the company's surplus that represents the net earnings, gains or profits (after deduction of all losses) that have not been distributed to shareholders as dividends or transferred to stated capital or capital surplus, or applied to other purposes permitted by law, but does not include unrealized appreciation of assets. AGM may pay dividends without the prior approval of the New York Superintendent of Financial Services ("New York Superintendent") that, together with all dividends declared or distributed by it during the preceding 12 months, does not exceed the lesser of 10% of its policyholders' surplus (as of its last annual or quarterly statement filed with the New York Superintendent) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGM to distribute as dividends without regulatory approval is estimated to be approximately \$236 million, of which approximately \$32 million is estimated to be available for distribution in the second quarter of 2016.

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Under Maryland's insurance law, AGC may, with prior notice to the Maryland Insurance Commissioner, pay an ordinary dividend that, together with all dividends paid in the prior 12 months, does not exceed 10% of its policyholders' surplus (as of the prior December 31) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGC to distribute as ordinary dividends is approximately \$79 million, of which approximately \$24 million is available for distribution in the second quarter of 2016.

MAC is a New York domiciled insurance company subject to the same dividend limitations described above for AGM. The Company does not currently anticipate that MAC will distribute any dividends.

For AG Re, any distribution (including repurchase of shares) of any share capital, contributed surplus or other statutory capital that would reduce its total statutory capital by 15% or more of its total statutory capital as set out in its previous year's financial statements requires the prior approval of the Bermuda Monetary Authority ("Authority"). Separately, dividends are paid out of an insurer's statutory surplus and cannot exceed that surplus. Further, annual dividends cannot exceed 25% of total statutory capital and surplus as set out in its previous year's financial statements, which is \$246 million, without AG Re certifying to the Authority that it will continue to meet required margins. Based on the foregoing limitations, in 2016 AG Re has the capacity to (i) make capital distributions in an aggregate amount up to \$127 million without the prior approval of the Authority and (ii) declare and pay dividends in an aggregate amount up to the limit of its outstanding statutory surplus, which is \$140 million. Such dividend capacity is further limited by the actual amount of AG Re's unencumbered assets, which amount changes from time to time due in part to collateral posting requirements. As of March 31, 2016, AG Re had unencumbered assets of approximately \$594 million.

U.K. company law prohibits each of AGE and AGUK from declaring a dividend to its shareholders unless it has "profits available for distribution." The determination of whether a company has profits available for distribution is based on its accumulated realized profits less its accumulated realized losses. While the U.K. insurance regulatory laws impose no statutory restrictions on a general insurer's ability to declare a dividend, the Prudential Regulation Authority's capital requirements may in practice act as a restriction on dividends. The Company does not expect AGE or AGUK to distribute any dividends at this time.

## Dividends and Surplus Notes

## By Insurance Company Subsidiaries

|                                          | First<br>Quarter<br>2016<br>(in<br>millions) |
|------------------------------------------|----------------------------------------------|
| Dividends paid by AGC to AGUS            | \$ — \$ 20                                   |
| Dividends paid by AGM to AGMH            | 95 66                                        |
| Dividends paid by AG Re to AGL           | 25 50                                        |
| Repayment of surplus note by AGM to AGMH | — 25                                         |

## 12. Income Taxes

## Overview

AGL, and its "Bermuda Subsidiaries," which consist of AG Re, AGRO, and Cedar Personnel Ltd., are not subject to any income, withholding or capital gains taxes under current Bermuda law. The Company has received an assurance

from the Minister of Finance in Bermuda that, in the event of any taxes being imposed, AGL and its Bermuda Subsidiaries will be exempt from taxation in Bermuda until March 31, 2035. AGL's U.S. and U.K. subsidiaries are subject to income taxes imposed by U.S. and U.K. authorities, respectively, and file applicable tax returns. In addition, AGRO, a Bermuda domiciled company and AGE, a U.K. domiciled company, have elected under Section 953(d) of the U.S. Internal Revenue Code to be taxed as a U.S. domestic corporation.

In November 2013, AGL became tax resident in the U.K. although it will remain a Bermuda-based company and its administrative and head office functions will continue to be carried on in Bermuda. As a U.K. tax resident company, AGL is required to file a corporation tax return with Her Majesty's Revenue & Customs ("HMRC"). AGL is subject to U.K. corporation tax in respect of its worldwide profits (both income and capital gains), subject to any applicable exemptions. The main rate of corporation tax remains at 20% for 2016. AGL has also registered in the U.K. to report its Value Added Tax

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("VAT") liability. The current rate of VAT is 20%. Assured Guaranty expects that the dividends AGL receives from its direct subsidiaries will be exempt from U.K. corporation tax due to the exemption in section 931D of the U.K. Corporation Tax Act 2009. In addition, any dividends paid by AGL to its shareholders should not be subject to any withholding tax in the U.K. The U.K. government implemented a tax regime for "controlled foreign companies" ("CFC regime") effective January 1, 2013. Assured Guaranty does not expect any profits of non-U.K. resident members of the group to be taxed under the CFC regime and has obtained a clearance from HMRC confirming this on the basis of current facts.

AGUS files a consolidated federal income tax return with AGC, AG Financial Products Inc. ("AGFP"), AG Analytics Inc., AGMH, beginning May 12, 2012 MAC and MAC Holdings, and beginning April 1, 2015 Radian Asset and Van American ("AGUS consolidated tax group"). Assured Guaranty Overseas US Holdings Inc. and its subsidiaries AGRO and AG Intermediary Inc., file their own consolidated federal income tax return.

## Provision for Income Taxes

The Company's provision for income taxes for interim financial periods is not based on an estimated annual effective rate due, for example, to the variability in fair value of its credit derivatives, which prevents the Company from projecting a reliable estimated annual effective tax rate and pretax income for the full year 2016. A discrete calculation of the provision is calculated for each interim period.

The effective tax rates reflect the proportion of income recognized by each of the Company's operating subsidiaries, with U.S. subsidiaries taxed at the U.S. marginal corporate income tax rate of 35%, U.K. subsidiaries taxed at the U.K. marginal corporate tax rate of 20% unless subject to U.S. tax by election or as a U.S. controlled foreign corporation, and no taxes for the Company's Bermuda subsidiaries unless subject to U.S. tax by election or as a U.S. controlled foreign corporation. For periods subsequent to April 1, 2015, the U.K. corporation tax rate has been reduced to 20% and will remain unchanged until April 1, 2017. For the period April 1, 2014 to April 1, 2015 the U.K. corporation tax rate was 21% resulting in a blended tax rate of 20.25% in 2015. The Company's overall effective tax rate fluctuates based on the distribution of income across jurisdictions.

A reconciliation of the difference between the provision for income taxes and the expected tax provision at statutory rates in taxable jurisdictions is presented below.

## Effective Tax Rate Reconciliation

|                                                                              | First Quarter |       |
|------------------------------------------------------------------------------|---------------|-------|
|                                                                              | 2016          | 2015  |
|                                                                              | (in millions) |       |
| Expected tax provision (benefit) at statutory rates in taxable jurisdictions | \$18          | \$77  |
| Tax-exempt interest                                                          | (13)          | (14)  |
| Change in liability for uncertain tax positions                              | 0             | 1     |
| Other                                                                        | 1             | 1     |
| Total provision (benefit) for income taxes                                   | \$6           | \$65  |
| Effective tax rate                                                           | 10.0%         | 24.2% |

The expected tax provision at statutory rates in taxable jurisdictions is calculated as the sum of pretax income in each jurisdiction multiplied by the statutory tax rate of the jurisdiction by which it will be taxed. Pretax income of the Company's subsidiaries which are not U.S. or U.K. domiciled but are subject to U.S. or U.K. tax by election, establishment of tax residency or as controlled foreign corporations, are included at the U.S. or U.K. statutory tax rate. Where there is a pretax loss in one jurisdiction and pretax income in another, the total combined expected tax rate may

be higher or lower than any of the individual statutory rates.



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The following table presents pretax income and revenue by jurisdiction.

## Pretax Income (Loss) by Tax Jurisdiction

|               | First<br>Quarter<br>2016 2015<br>(in millions) |       |
|---------------|------------------------------------------------|-------|
| United States | \$55                                           | \$223 |
| Bermuda       | 17                                             | 50    |
| U.K.          | (7 )                                           | (7 )  |
| Total         | \$65                                           | \$266 |

## Revenue by Tax Jurisdiction

|               | First Quarter<br>2016 2015<br>(in millions) |       |
|---------------|---------------------------------------------|-------|
| United States | \$205                                       | \$300 |
| Bermuda       | 42                                          | 73    |
| U.K.          | (2 )                                        | (4 )  |
| Total         | \$245                                       | \$369 |

Pretax income by jurisdiction may be disproportionate to revenue by jurisdiction to the extent that insurance losses incurred are disproportionate.

## Valuation Allowance

As part of the Radian Asset Acquisition, the Company acquired \$11 million of foreign tax credits (“FTC”) which will expire between 2018 and 2020. After reviewing positive and negative evidence, the Company came to the conclusion that it is more likely than not that the FTC will not be utilized, and therefore recorded a valuation allowance with respect to this tax attribute.

The Company came to the conclusion that it is more likely than not that the remaining net deferred tax asset will be fully realized after weighing all positive and negative evidence available as required under GAAP. The positive evidence that was considered included the cumulative income the Company has earned over the last three years, and the significant unearned premium income to be included in taxable income. The positive evidence outweighs any negative evidence that exists. As such, the Company believes that no valuation allowance is necessary in connection with this deferred tax asset. The Company will continue to analyze the need for a valuation allowance on a quarterly basis.

## Audits

AGUS has open tax years with the U.S. Internal Revenue Service (“IRS”) for 2009 forward and is currently under audit for the 2009-2012 tax years. Assured Guaranty Oversees US Holdings Inc. has open tax years of 2012 forward. The Company's U.K. subsidiaries are not currently under examination and have open tax years of 2014 forward.

## Uncertain Tax Positions

The Company's policy is to recognize interest and penalties related to uncertain tax positions in income tax expense and has accrued \$0.4 million for First Quarter 2016 and \$1 million for 2015. As of March 31, 2016 and December 31, 2015, the Company has accrued \$5.8 million and \$5.4 million of interest, respectively.

The total amount of unrecognized tax benefits as of March 31, 2016 and December 31, 2015, that would affect the effective tax rate, if recognized, was \$46 million and \$45 million, respectively.

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13. Reinsurance and Other Monoline Exposures

The Company assumes exposure on insured obligations (“Assumed Business”) and may cede portions of its exposure on obligations it has insured (“Ceded Business”) in exchange for premiums, net of ceding commissions. The Company historically entered into ceded reinsurance contracts in order to obtain greater business diversification and reduce the net potential loss from large risks.

Assumed and Ceded Business

The Company assumes business from other monoline financial guaranty companies. Under these relationships, the Company assumes a portion of the ceding company’s insured risk in exchange for a premium. The Company may be exposed to risk in this portfolio in that the Company may be required to pay losses without a corresponding premium in circumstances where the ceding company is experiencing financial distress and is unable to pay premiums. The Company’s facultative and treaty agreements are generally subject to termination at the option of the ceding company:

- if the Company fails to meet certain financial and regulatory criteria and to maintain a specified minimum financial strength rating, or

- upon certain changes of control of the Company.

Upon termination under these conditions, the Company may be required (under some of its reinsurance agreements) to return to the ceding company unearned premiums (net of ceding commissions) and loss reserves calculated on a statutory basis of accounting, attributable to reinsurance assumed pursuant to such agreements after which the Company would be released from liability with respect to the Assumed Business.

Upon the occurrence of the conditions set forth in the first bullet above, whether or not an agreement is terminated, the Company may be required to obtain a letter of credit or alternative form of security to collateralize its obligation to perform under such agreement or it may be obligated to increase the level of ceding commission paid.

The downgrade of the financial strength ratings of AG Re or of AGC gives certain ceding companies the right to recapture business they had ceded to AG Re and AGC, which would lead to a reduction in the Company's unearned premium reserve and related earnings on such reserve. With respect to a significant portion of the Company's in-force financial guaranty assumed business, based on AG Re's and AGC's current ratings and subject to the terms of each reinsurance agreement, the third party ceding company may have the right to recapture business it had ceded to AG Re and/or AGC, and in connection therewith, to receive payment from AG Re or AGC of an amount equal to the statutory unearned premium (net of ceding commissions) and statutory loss reserves (if any) associated with that business, plus, in certain cases, an additional ceding commission. As of March 31, 2016, if each third party insurer ceding business to AG Re and/or AGC had a right to recapture such business, and chose to exercise such right, the aggregate amounts that AG Re and AGC could be required to pay to all such companies would be approximately \$50 million and \$33 million, respectively.

The Company has Ceded Business to non-affiliated companies to limit its exposure to risk. Under these relationships, the Company ceded a portion of its insured risk in exchange for a premium paid to the reinsurer. The Company remains primarily liable for all risks it directly underwrites and is required to pay all gross claims. It then seeks reimbursement from the reinsurer for its proportionate share of claims. The Company may be exposed to risk for this exposure if it were required to pay the gross claims and not be able to collect ceded claims from an assuming company experiencing financial distress. A number of the financial guaranty insurers to which the Company has ceded par have experienced financial distress and been downgraded by the rating agencies as a result. In addition, state insurance regulators have intervened with respect to some of these insurers. The Company’s ceded contracts generally allow the

Company to recapture Ceded Business after certain triggering events, such as reinsurer downgrades.

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The following table presents the components of premiums and losses reported in the consolidated statement of operations and the contribution of the Company's Assumed and Ceded Businesses.

## Effect of Reinsurance on Statement of Operations

|                   | First Quarter |       |
|-------------------|---------------|-------|
|                   | 2016          | 2015  |
|                   | (in millions) |       |
| Premiums Written: |               |       |
| Direct            | \$21          | \$29  |
| Assumed           | (2 )          | 3     |
| Ceded             | (17 )         | 0     |
| Net               | \$2           | \$32  |
| Premiums Earned:  |               |       |
| Direct            | \$190         | \$148 |
| Assumed           | 8             | 10    |
| Ceded             | (15 )         | (16 ) |
| Net               | \$183         | \$142 |
| Loss and LAE:     |               |       |
| Direct            | \$109         | \$26  |
| Assumed           | (14 )         | (7 )  |
| Ceded             | (5 )          | (1 )  |
| Net               | \$90          | \$18  |

## Other Monoline Exposures

In addition to assumed and ceded reinsurance arrangements, the Company may also have exposure to some financial guaranty reinsurers (i.e., monolines) in other areas. Second-to-pay insured par outstanding represents transactions the Company has insured that were previously insured by other monolines. The Company underwrites such transactions based on the underlying insured obligation without regard to the primary insurer. Another area of exposure is in the investment portfolio where the Company holds fixed-maturity securities that are wrapped by monolines and whose value may change based on the rating of the monoline. As of March 31, 2016, based on fair value, the Company had fixed-maturity securities in its investment portfolio consisting of \$157 million insured by National Public Finance Guarantee Corporation ("National"), \$139 million insured by Ambac and \$8 million insured by other guarantors. In addition, the Company acquired bonds for loss mitigation or other risk management purposes. As of March 31, 2016 these bonds had a fair value of \$247 million insured by MBIA Insurance Corp. and \$127 million insured by FGIC UK Limited.

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## Exposure by Reinsurer

| Reinsurer                                           | Ratings at<br>May 3, 2016      |                            | Par Outstanding (1)<br>As of March 31, 2016 |                                                 |                            |
|-----------------------------------------------------|--------------------------------|----------------------------|---------------------------------------------|-------------------------------------------------|----------------------------|
|                                                     | Moody's<br>Reinsurer<br>Rating | S&P<br>Reinsurer<br>Rating | Ceded Par<br>Outstanding                    | Pay Insured<br>Second-to-<br>Pay<br>Outstanding | Assumed Par<br>Outstanding |
| (dollars in millions)                               |                                |                            |                                             |                                                 |                            |
| American Overseas Reinsurance Company Limited (2)   | WR (3)                         | WR                         | \$4,960                                     | \$ —                                            | \$ 30                      |
| Tokio Marine & Nichido Fire Insurance Co., Ltd. (2) | Aa3 (4)                        | A+ (4)                     | 4,171                                       | —                                               | —                          |
| Syncora Guarantee Inc. (2)                          | WR                             | WR                         | 2,411                                       | 1,319                                           | 700                        |
| Mitsui Sumitomo Insurance Co. Ltd. (2)              | A1                             | A+ (4)                     | 1,718                                       | —                                               | —                          |
| ACA Financial Guaranty Corp.                        | NR (5)                         | WR                         | 700                                         | 38                                              | —                          |
| Ambac                                               | WR                             | WR                         | 117                                         | 3,892                                           | 9,589                      |
| National (6)                                        | A3                             | AA-                        | —                                           | 5,139                                           | 5,065                      |
| MBIA                                                | (7)                            | (7)                        | —                                           | 1,591                                           | 428                        |
| FGIC                                                | (8)                            | (8)                        | —                                           | 1,437                                           | 636                        |
| Ambac Assurance Corp. Segregated Account            | NR                             | NR                         | —                                           | 86                                              | 823                        |
| CIFG Assurance North America Inc.                   | WR                             | WR                         | —                                           | 43                                              | 2,784                      |
| Other (2)                                           | Various                        | Various                    | 76                                          | 776                                             | 128                        |
| Total                                               |                                |                            | \$14,153                                    | \$ 14,321                                       | \$ 20,183                  |

(1) Includes par related to insured credit derivatives.

(2) The total collateral posted by all non-affiliated reinsurers required or agreeing to post collateral as of March 31, 2016 was approximately \$436 million.

(3) Represents "Withdrawn Rating."

(4) The Company benefits from trust arrangements that satisfy the triple-A credit requirement of S&P and/or Moody's.

(5) Represents "Not Rated."

(6) Rated AA+ by KBRA.

(7) MBIA includes subsidiaries MBIA Insurance Corp. rated B by S&P and B3 by Moody's and MBIA U.K. Insurance Ltd. rated BB by S&P and Ba2 by Moody's.

(8) FGIC includes subsidiaries Financial Guaranty Insurance Company and FGIC UK Limited both of which had their ratings withdrawn by rating agencies.

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## Amounts Due (To) From Reinsurers

As of March 31, 2016

|                                                 | Assumed<br>Premium, net<br>of Commissions | Ceded<br>Premium, net<br>of Commissions | Assumed<br>Expected<br>Loss to<br>be Paid | Ceded<br>Expected<br>Loss to<br>be Paid |
|-------------------------------------------------|-------------------------------------------|-----------------------------------------|-------------------------------------------|-----------------------------------------|
|                                                 | (in millions)                             |                                         |                                           |                                         |
| American Overseas Reinsurance Company Limited   | \$—                                       | \$ (6 )                                 | \$ —                                      | \$ 25                                   |
| Tokio Marine & Nichido Fire Insurance Co., Ltd. | —                                         | (11 )                                   | —                                         | 44                                      |
| Syncora Guarantee Inc.                          | 15                                        | (21 )                                   | —                                         | 5                                       |
| Mitsui Sumitomo Insurance Co. Ltd.              | —                                         | (3 )                                    | —                                         | 18                                      |
| Ambac                                           | 39                                        | —                                       | (3 )                                      | —                                       |
| National                                        | 6                                         | —                                       | (4 )                                      | —                                       |
| MBIA                                            | 5                                         | —                                       | (10 )                                     | —                                       |
| FGIC                                            | 4                                         | —                                       | (15 )                                     | —                                       |
| Ambac Assurance Corp. Segregated Account        | 10                                        | —                                       | (46 )                                     | —                                       |
| CIFG Assurance North America Inc.               | 0                                         | —                                       | (63 )                                     | —                                       |
| Other                                           | —                                         | (12 )                                   | —                                         | —                                       |
| Total                                           | \$79                                      | \$ (53 )                                | \$ (141 )                                 | \$ 92                                   |

## Excess of Loss Reinsurance Facility

AGC, AGM and MAC entered into a \$360 million aggregate excess of loss reinsurance facility with a number of reinsurers, effective as of January 1, 2016. This facility replaces a similar \$450 million aggregate excess of loss reinsurance facility that AGC, AGM and MAC had entered into effective January 1, 2014 and which terminated on December 31, 2015. The new facility covers losses occurring either from January 1, 2016 through December 31, 2023, or January 1, 2017 through December 31, 2024, at the option of AGC, AGM and MAC. It terminates on January 1, 2018, unless AGC, AGM and MAC choose to extend it. The new facility covers certain U.S. public finance credits insured or reinsured by AGC, AGM and MAC as of September 30, 2015, excluding credits that were rated non-investment grade as of December 31, 2015 by Moody's or S&P or internally by AGC, AGM or MAC and is subject to certain per credit limits. Among the credits excluded are those associated with the Commonwealth of Puerto Rico and its related authorities and public corporations. The new facility attaches when AGC's, AGM's and MAC's net losses (net of AGC's and AGM's reinsurance (including from affiliates) and net of recoveries) exceed \$1.25 billion in the aggregate. The new facility covers a portion of the next \$400 million of losses, with the reinsurers assuming pro rata in the aggregate \$360 million of the \$400 million of losses and AGC, AGM and MAC jointly retaining the remaining \$40 million. The reinsurers are required to be rated at least AA- or to post collateral sufficient to provide AGM, AGC and MAC with the same reinsurance credit as reinsurers rated AA-. AGM, AGC and MAC are obligated to pay the reinsurers their share of recoveries relating to losses during the coverage period in the covered portfolio. AGC, AGM and MAC paid approximately \$9 million of premiums in 2016 for the term January 1, 2016 through December 31, 2016 and deposited approximately \$9 million of securities into trust accounts for the benefit of the reinsurers to be used to pay the premium for January 1, 2017 through December 31, 2017. The main differences between the new facility and the prior facility that terminated on December 31, 2015 are the reinsurance attachment point (\$1.25 billion versus \$1.5 billion), the total reinsurance coverage (\$360 million part of \$400 million versus \$450 million part of \$500 million) and the annual premium (\$9 million versus \$19 million).





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### 14. Commitments and Contingencies

#### Legal Proceedings

Lawsuits arise in the ordinary course of the Company's business. It is the opinion of the Company's management, based upon the information available, that the expected outcome of litigation against the Company, individually or in the aggregate, will not have a material adverse effect on the Company's financial position or liquidity, although an adverse resolution of litigation against the Company in a fiscal quarter or year could have a material adverse effect on the Company's results of operations in a particular quarter or year.

In addition, in the ordinary course of their respective businesses, certain of the Company's subsidiaries assert claims in legal proceedings against third parties to recover losses paid in prior periods or prevent losses in the future. For example, as described in the "Recovery Litigation" section of Note 5, Expected Loss to be Paid, in January 2016 the Company commenced an action for declaratory judgment and injunctive relief in the U.S. District Court for the District of Puerto Rico to invalidate executive orders issued by the Governor of Puerto Rico directing the retention or transfer of certain taxes and revenues pledged to secure the payment of certain bonds insured by the Company. Also, in December 2008, the Company filed a claim in the Supreme Court of the State of New York against an investment manager in a transaction it insured alleging breach of fiduciary duty, gross negligence and breach of contract. The amounts, if any, the Company will recover in proceedings to recover losses are uncertain, and recoveries, or failure to obtain recoveries, in any one or more of these proceedings during any quarter or year could be material to the Company's results of operations in that particular quarter or year.

The Company establishes accruals for litigation and regulatory matters to the extent it is probable that a loss has been incurred and the amount of that loss can be reasonably estimated. For litigation and regulatory matters where a loss may be reasonably possible, but not probable, or is probable but not reasonably estimable, no accrual is established, but if the matter is material, it is disclosed, including matters discussed below. The Company reviews relevant information with respect to its litigation and regulatory matters on a quarterly, and annual basis and updates its accruals, disclosures and estimates of reasonably possible loss based on such reviews.

#### Litigation

##### Proceedings Relating to the Company's Financial Guaranty Business

The Company receives subpoenas duces tecum and interrogatories from regulators from time to time.

On November 28, 2011, Lehman Brothers International (Europe) (in administration) ("LBIE") sued AGFP, an affiliate of AGC which in the past had provided credit protection to counterparties under credit default swaps. AGC acts as the credit support provider of AGFP under these credit default swaps. LBIE's complaint, which was filed in the Supreme Court of the State of New York, alleged that AGFP improperly terminated nine credit derivative transactions between LBIE and AGFP and improperly calculated the termination payment in connection with the termination of 28 other credit derivative transactions between LBIE and AGFP. Following defaults by LBIE, AGFP properly terminated the transactions in question in compliance with the agreement between AGFP and LBIE, and calculated the termination payment properly. AGFP calculated that LBIE owes AGFP approximately \$29 million in connection with the termination of the credit derivative transactions, whereas LBIE asserted in the complaint that AGFP owes LBIE a termination payment of approximately \$1.4 billion. On February 3, 2012, AGFP filed a motion to dismiss certain of the counts in the complaint, and on March 15, 2013, the court granted AGFP's motion to dismiss the count relating to improper termination of the nine credit derivative transactions and denied AGFP's motion to dismiss the counts relating to the remaining transactions. On February 22, 2016, AGFP filed a motion for summary judgment on the remaining causes of action asserted by LBIE and on AGFP's counterclaims. LBIE's administrators disclosed in an

April 10, 2015 report to LBIE's unsecured creditors that LBIE's valuation expert has calculated LBIE's damages in aggregate for the 28 transactions to range between a minimum of approximately \$200 million and a maximum of approximately \$500 million, depending on what adjustment, if any, is made for AGFP's credit risk and excluding any applicable interest. Notwithstanding the range calculated by LBIE's valuation expert, the Company cannot reasonably estimate the possible loss, if any, that may arise from this lawsuit.

On September 25, 2013, Wells Fargo Bank, N.A., as trust administrator of the MASTR Adjustable Rate Mortgages Trust 2007-3, filed an interpleader complaint in the U.S. District Court for the Southern District of New York against AGM, among others, relating to the right of AGM to be reimbursed from certain cashflows for principal claims paid in respect of insured certificates. The Company estimates that an adverse outcome to the interpleader proceeding could increase losses on the transaction by approximately \$10 - \$20 million, net of expected settlement payments and reinsurance in force.

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### Proceedings Resolved Since December 31, 2015

On May 28, 2014, Houston Casualty Company Europe, Seguros y Reseguros, S.A. (“HCCE”) notified Radian Asset that it was demanding arbitration against Radian Asset in connection with housing cooperative losses presented to Radian Asset by HCCE under several years of quota-share surety reinsurance contracts. Through November 30, 2015, HCCE had presented AGC, as successor to Radian Asset, with approximately €15 million in claims. In January 2016, Assured Guaranty and HCCE settled all the claims related to the Spanish housing cooperative losses.

### Proceedings Related to AGMH’s Former Financial Products Business

The following is a description of legal proceedings involving AGMH’s former Financial Products Business. Although the Company did not acquire AGMH’s former Financial Products Business, which included AGMH’s former GIC business, medium term notes business and portions of the leveraged lease businesses, certain legal proceedings relating to those businesses are against entities that the Company did acquire. While Dexia SA and Dexia Crédit Local S.A., jointly and severally, have agreed to indemnify the Company against liability arising out of the proceedings described below, such indemnification might not be sufficient to fully hold the Company harmless against any injunctive relief or civil or criminal sanction that is imposed against AGMH or its subsidiaries.

### Governmental Investigations into Former Financial Products Business

AGMH and/or AGM have received subpoenas duces tecum and interrogatories or civil investigative demands from the Attorneys General of the States of Connecticut, Florida, Illinois, Massachusetts, Missouri, New York, Texas and West Virginia relating to their investigations of alleged bid rigging of municipal GICs. AGMH has been responding to such requests. AGMH may receive additional inquiries from these or other regulators and expects to provide additional information to such regulators regarding their inquiries in the future. In addition, AGMH received a subpoena from the Antitrust Division of the Department of Justice in November 2006 issued in connection with an ongoing criminal investigation of bid rigging of awards of municipal GICs and other municipal derivatives. Pursuant to that subpoena, AGMH has furnished to the Department of Justice records and other information with respect to AGMH’s municipal GIC business. The ultimate loss that may arise from these investigations remains uncertain.

### Lawsuits Relating to Former Financial Products Business

During 2008, nine putative class action lawsuits were filed in federal court alleging federal antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. These cases have been coordinated and consolidated for pretrial proceedings in the U.S. District Court for the Southern District of New York as MDL 1950, In re Municipal Derivatives Antitrust Litigation, Case No. 1:08-cv-2516 (“MDL 1950”). Five of these cases named both AGMH and AGM: (a) Hinds County, Mississippi v. Wachovia Bank, N.A.; (b) Fairfax County, Virginia v. Wachovia Bank, N.A.; (c) Central Bucks School District, Pennsylvania v. Wachovia Bank, N.A.; (d) Mayor and City Council of Baltimore, Maryland v. Wachovia Bank, N.A.; and (e) Washington County, Tennessee v. Wachovia Bank, N.A. In April 2009, the MDL 1950 court granted the defendants’ motion to dismiss on the federal claims for these five cases, but granted leave for the plaintiffs to file an amended complaint. The Corrected Third Consolidated Amended Class Action Complaint, filed on October 9, 2013, lists neither AGM nor AGMH as a named defendant or a co-conspirator. The complaint generally seeks unspecified monetary damages, interest, attorneys’ fees and other costs. The other four cases named AGMH (but not AGM) and also alleged that the defendants violated California state antitrust law and common law by engaging in illegal bid-rigging and market allocation, thereby depriving the cities or municipalities of competition in the awarding of GICs and ultimately resulting in the cities paying higher fees for these products: (f) City of Oakland, California v. AIG Financial Products Corp.; (g) County of Alameda, California v. AIG Financial Products Corp.; (h) City of Fresno, California v. AIG Financial Products Corp.; and (i) Fresno County Financing

Authority v. AIG Financial Products Corp. When the four plaintiffs filed a consolidated complaint in September 2009, the plaintiffs did not name AGMH as a defendant. However, the complaint does describe some of AGMH's and AGM's activities. The consolidated complaint generally seeks unspecified monetary damages, interest, attorneys' fees and other costs. In April 2010, the MDL 1950 court granted in part and denied in part the named defendants' motions to dismiss this consolidated complaint. On September 22, 2015, the remaining parties to the putative class action reported to the MDL 1950 Court that settlements in principle had been reached, and a motion for preliminary approval of those putative class claims was filed on February 24, 2016. The parties have reported that final settlement with those remaining defendants would resolve the putative class case. The settlement fairness hearing for those putative class cases is scheduled for July 8, 2016. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from these lawsuits.

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In 2008, AGMH and AGM also were named in five non-class action lawsuits originally filed in the California Superior Courts alleging violations of California law related to the municipal derivatives industry: (a) City of Los Angeles, California v. Bank of America, N.A.; (b) City of Stockton, California v. Bank of America, N.A.; (c) County of San Diego, California v. Bank of America, N.A.; (d) County of San Mateo, California v. Bank of America, N.A.; and (e) County of Contra Costa, California v. Bank of America, N.A. Amended complaints in these actions were filed in September 2009, adding a federal antitrust claim and naming AGM (but not AGMH) and AGUS, among other defendants. These cases have been transferred to the Southern District of New York and consolidated with MDL 1950 for pretrial proceedings. In late 2009, AGM and AGUS, among other defendants, were named in six additional non-class action cases filed in federal court, which also have been coordinated and consolidated for pretrial proceedings with MDL 1950; one was voluntarily dismissed with prejudice in October 2010, leaving five that are currently pending: (f) City of Riverside, California v. Bank of America, N.A.; (g) Los Angeles World Airports v. Bank of America, N.A.; (h) Redevelopment Agency of the City of Stockton v. Bank of America, N.A.; (i) Sacramento Suburban Water District v. Bank of America, N.A.; and (j) County of Tulare, California v. Bank of America, N.A. The MDL 1950 court denied AGM and AGUS's motions to dismiss the eleven complaints that were pending as of April 2010. Amended complaints were filed in May 2010. The complaints in these lawsuits generally seek or sought unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from the remaining lawsuits.

In May 2010, AGM and AGUS, among other defendants, were named in five additional non-class action cases filed in federal court in California: (a) City of Richmond, California v. Bank of America, N.A. (filed on May 18, 2010, N.D. California); (b) City of Redwood City, California v. Bank of America, N.A. (filed on May 18, 2010, N.D. California); (c) Redevelopment Agency of the City and County of San Francisco, California v. Bank of America, N.A. (filed on May 21, 2010, N.D. California); (d) East Bay Municipal Utility District, California v. Bank of America, N.A. (filed on May 18, 2010, N.D. California); and (e) City of San Jose and the San Jose Redevelopment Agency, California v. Bank of America, N.A. (filed on May 18, 2010, N.D. California). These cases have also been transferred to the Southern District of New York and consolidated with MDL 1950 for pretrial proceedings. In September 2010, AGM and AGUS, among other defendants, were named in a sixth additional non-class action filed in federal court in New York, but which alleges violation of New York's Donnelly Act in addition to federal antitrust law: Active Retirement Community, Inc. d/b/a Jefferson's Ferry v. Bank of America, N.A. (filed on September 21, 2010, E.D. New York), which has also been transferred to the Southern District of New York and consolidated with MDL 1950 for pretrial proceedings. In December 2010, AGM and AGUS, among other defendants, were named in a seventh additional non-class action filed in federal court in the Central District of California, Los Angeles Unified School District v. Bank of America, N.A., and in an eighth additional non-class action filed in federal court in the Southern District of New York, Kendal on Hudson, Inc. v. Bank of America, N.A. These cases also have been consolidated with MDL 1950 for pretrial proceedings. The complaints in these lawsuits generally seek unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from these lawsuits.

In January 2011, AGM and AGUS, among other defendants, were named in an additional non-class action case filed in federal court in New York, which alleges violation of New York's Donnelly Act in addition to federal antitrust law: Peconic Landing at Southold, Inc. v. Bank of America, N.A. This case has been consolidated with MDL 1950 for pretrial proceedings. The complaint in this lawsuit generally seeks unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from this lawsuit.

In September 2009, the Attorney General of the State of West Virginia filed a lawsuit (Circuit Ct. Mason County, W. Va.) against Bank of America, N.A. alleging West Virginia state antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. An amended complaint in this action was filed in June 2010, adding a

federal antitrust claim and naming AGM (but not AGMH) and AGUS, among other defendants. This case has been removed to federal court as well as transferred to the S.D.N.Y. and consolidated with MDL 1950 for pretrial proceedings. AGM and AGUS answered West Virginia's Second Amended Complaint on November 11, 2013. The complaint in this lawsuit generally seeks civil penalties, unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from this lawsuit.

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## 15. Long-Term Debt and Credit Facilities

The principal and carrying values of the Company's long-term debt are presented in the table below.

## Principal and Carrying Amounts of Debt

|                                                  | As of March 31,<br>2016 |                   | As of December<br>31, 2015 |                   |
|--------------------------------------------------|-------------------------|-------------------|----------------------------|-------------------|
|                                                  | Principal               | Carrying<br>Value | Principal                  | Carrying<br>Value |
|                                                  | (in millions)           |                   |                            |                   |
| AGUS:                                            |                         |                   |                            |                   |
| 7% Senior Notes                                  | \$200                   | \$ 197            | \$200                      | \$ 197            |
| 5% Senior Notes                                  | 500                     | 496               | 500                        | 495               |
| Series A Enhanced Junior Subordinated Debentures | 150                     | 150               | 150                        | 150               |
| Total AGUS                                       | 850                     | 843               | 850                        | 842               |
| AGMH:                                            |                         |                   |                            |                   |
| 67/8% QUIBS                                      | 100                     | 69                | 100                        | 69                |
| 6.25% Notes                                      | 230                     | 140               | 230                        | 140               |
| 5.6% Notes                                       | 100                     | 56                | 100                        | 56                |
| Junior Subordinated Debentures                   | 300                     | 182               | 300                        | 180               |
| Total AGMH                                       | 730                     | 447               | 730                        | 445               |
| AGM:                                             |                         |                   |                            |                   |
| Notes Payable                                    | 11                      | 12                | 12                         | 13                |
| Total AGM                                        | 11                      | 12                | 12                         | 13                |
| Total                                            | \$1,591                 | \$ 1,302          | \$ 1,592                   | \$ 1,300          |

## Recourse Credit Facilities

## 2009 Strip Coverage Facility

In connection with the Company's acquisition of AGMH and its subsidiaries from Dexia Holdings Inc., AGM agreed to retain the risks relating to the debt and strip policy portions of the leveraged lease business. The liquidity risk to AGM related to the strip policy portion of the leveraged lease business is mitigated by the strip coverage facility described below.

In a leveraged lease transaction, a tax-exempt entity (such as a transit agency) transfers tax benefits to a tax-paying entity by transferring ownership of a depreciable asset, such as subway cars. The tax-exempt entity then leases the asset back from its new owner.

If the lease is terminated early, the tax-exempt entity must make an early termination payment to the lessor. A portion of this early termination payment is funded from monies that were pre-funded and invested at the closing of the leveraged lease transaction (along with earnings on those invested funds). The tax-exempt entity is obligated to pay the remaining, unfunded portion of this early termination payment (known as the "strip coverage") from its own sources. AGM issued financial guaranty insurance policies (known as "strip policies") that guaranteed the payment of these unfunded strip coverage amounts to the lessor, in the event that a tax-exempt entity defaulted on its obligation to pay this portion of its early termination payment. AGM can then seek reimbursement of its strip policy payments from the tax-exempt entity, and can also sell the transferred depreciable asset and reimburse itself from the sale proceeds.

Currently, all the leveraged lease transactions in which AGM acts as strip coverage provider are breaching a rating trigger related to AGM and are subject to early termination. However, early termination of a lease does not result in a draw on the AGM policy if the tax-exempt entity makes the required termination payment. If all the leases were to terminate early and the tax-exempt entities do not make the required early termination payments, then AGM would be exposed to possible liquidity claims on gross exposure of approximately \$1.1 billion as of March 31, 2016. To date, none of the leveraged lease transactions that involve AGM has experienced an early termination due to a lease default and a claim on the AGM policy. It is difficult to determine the probability that AGM will have to pay strip provider claims or the likely aggregate amount of such claims. At March 31, 2016, approximately \$1.4 billion of cumulative strip par exposure had been terminated since 2008 on a consensual basis. The consensual terminations have resulted in no claims on AGM.



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On July 1, 2009, AGM and Dexia Crédit Local S.A., acting through its New York Branch (“Dexia Crédit Local (NY)”), entered into a credit facility (the “Strip Coverage Facility”). Under the Strip Coverage Facility, Dexia Crédit Local (NY) agreed to make loans to AGM to finance all draws made by lessors on AGM strip policies that were outstanding as of November 13, 2008, up to the commitment amount, which is currently \$495 million.

Fundings under this facility are subject to certain conditions precedent, and their repayment is collateralized by a security interest that AGM granted to Dexia Crédit Local (NY) in amounts that AGM recovers—from the tax-exempt entity, or from asset sale proceeds—following its payment of strip policy claims. On June 30, 2014, AGM and Dexia Crédit Local (NY) agreed to shorten the duration of the facility. Accordingly, the Strip Coverage Facility will terminate upon the earliest to occur of an AGM change of control, the reduction of the commitment amount to \$0 in accordance with the terms of the facility, and June 30, 2024 (rather than the original maturity date of January 31, 2042).

The Strip Coverage Facility’s financial covenants require that AGM and its subsidiaries maintain:

- a maximum debt-to-capital ratio of 30%; and

a minimum net worth of 75% of consolidated net worth as of July 1, 2009, plus, beginning June 30, 2015 and on each anniversary of such date, an amount equal to the product of (i) 25% of the aggregate consolidated net income (or loss) for the period beginning July 2, 2009 and ending on June 30, 2014 and (ii) a fraction, the numerator of which is the commitment amount as of the relevant calculation date and the denominator of which is \$1 billion.

The Company was in compliance with all financial covenants as of March 31, 2016.

The Strip Coverage Facility contains restrictions on AGM, including, among other things, in respect of its ability to incur debt, permit liens, pay dividends or make distributions, dissolve or become party to a merger or consolidation. Most of these restrictions are subject to exceptions. The Strip Coverage Facility has customary events of default, including (subject to certain materiality thresholds and grace periods) payment default, bankruptcy or insolvency proceedings and cross-default to other debt agreements.

As of March 31, 2016, no amounts were outstanding under this facility, nor have there been any borrowings during the life of this facility.

### Intercompany Credit Facility and Intercompany Debt

On October 25, 2013, AGL, as borrower, and AGUS, as lender, entered into a revolving credit facility pursuant to which AGL may, from time to time, borrow for general corporate purposes. Under the credit facility, AGUS committed to lend a principal amount not exceeding \$225 million in the aggregate. Such commitment terminates on October 25, 2018 (the “loan termination date”). The unpaid principal amount of each loan will bear interest at a fixed rate equal to 100% of the then applicable Federal short-term or mid-term interest rate, as the case may be, as determined under Internal Revenue Code Sec. 1274(d), and interest on all loans will be computed for the actual number of days elapsed on the basis of a year consisting of 360 days. Accrued interest on all loans will be paid on the last day of each June and December, beginning on December 31, 2013, and at maturity. AGL must repay the then unpaid principal amounts of the loans by the third anniversary of the loan termination date. No amounts are currently outstanding under the credit facility.

In addition, in 2012 AGUS borrowed \$90 million from its affiliate AGRO to fund the acquisition of MAC. That loan remained outstanding as of March 31, 2016.

Committed Capital Securities

On April 8, 2005, AGC entered into separate agreements (the “Put Agreements”) with four custodial trusts (each, a “Custodial Trust”) pursuant to which AGC may, at its option, cause each of the Custodial Trusts to purchase up to \$50 million of perpetual preferred stock of AGC (the “AGC Preferred Stock”). The custodial trusts were created as a vehicle for providing capital support to AGC by allowing AGC to obtain immediate access to new capital at its sole discretion at any time through the exercise of the put option. If the put options were exercised, AGC would receive \$200 million in return for the issuance of its own perpetual preferred stock, the proceeds of which may be used for any purpose, including the payment of claims. The put options have not been exercised through the date of this filing.

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Distributions on the AGC CCS are determined pursuant to an auction process. Beginning on April 7, 2008 this auction process failed, thereby increasing the annualized rate on the AGC CCS to one-month LIBOR plus 250 basis points.

In June 2003, \$200 million of "AGM CPS", money market preferred trust securities, were issued by trusts created for the primary purpose of issuing the AGM CPS, investing the proceeds in high-quality commercial paper and selling put options to AGM, allowing AGM to issue the trusts non-cumulative redeemable perpetual preferred stock (the "AGM Preferred Stock") of AGM in exchange for cash. There are four trusts, each with an initial aggregate face amount of \$50 million. These trusts hold auctions every 28 days, at which time investors submit bid orders to purchase AGM CPS. If AGM were to exercise a put option, the applicable trust would transfer the portion of the proceeds attributable to principal received upon maturity of its assets, net of expenses, to AGM in exchange for AGM Preferred Stock. AGM pays a floating put premium to the trusts, which represents the difference between the commercial paper yield and the winning auction rate (plus all fees and expenses of the trust). If an auction does not attract sufficient clearing bids, however, the auction rate is subject to a maximum rate of one-month LIBOR plus 200 basis points for the next succeeding distribution period. Beginning in August 2007, the AGM CPS required the maximum rate for each of the relevant trusts. AGM continues to have the ability to exercise its put option and cause the related trusts to purchase AGM Preferred Stock. The trusts provide AGM access to new capital at its sole discretion through the exercise of the put options. As of March 31, 2016 the put option had not been exercised.

The Company does not consider itself to be the primary beneficiary of the trusts. See Note 7, Fair Value Measurement, –Other Assets–Committed Capital Securities, for a fair value measurement discussion.

## 16. Earnings Per Share

## Computation of Earnings Per Share

|                                                                                                                | First Quarter |        |
|----------------------------------------------------------------------------------------------------------------|---------------|--------|
|                                                                                                                | 2016          | 2015   |
|                                                                                                                | (in millions) |        |
| Basic earnings per share ("EPS"):                                                                              |               |        |
| Net income (loss) attributable to AGL                                                                          | \$59          | \$201  |
| Less: Distributed and undistributed income (loss) available to nonvested shareholders                          | 1             | 0      |
| Distributed and undistributed income (loss) available to common shareholders of AGL and subsidiaries, basic    | \$58          | \$201  |
| Basic shares                                                                                                   | 136.2         | 155.8  |
| Basic EPS                                                                                                      | \$0.43        | \$1.29 |
| Diluted EPS:                                                                                                   |               |        |
| Distributed and undistributed income (loss) available to common shareholders of AGL and subsidiaries, basic    | \$58          | \$201  |
| Plus: Re-allocation of undistributed income (loss) available to nonvested shareholders of AGL and subsidiaries | 0             | 0      |
| Distributed and undistributed income (loss) available to common shareholders of AGL and subsidiaries, diluted  | \$58          | \$201  |
| Basic shares                                                                                                   | 136.2         | 155.8  |
| Dilutive securities:                                                                                           |               |        |
| Options and restricted stock awards                                                                            | 0.8           | 1.0    |
| Diluted shares                                                                                                 | 137.0         | 156.8  |
| Diluted EPS                                                                                                    | \$0.43        | \$1.28 |

|                                                                                                 |     |     |
|-------------------------------------------------------------------------------------------------|-----|-----|
| Potentially dilutive securities excluded from computation of EPS because of antidilutive effect | 0.8 | 0.7 |
|-------------------------------------------------------------------------------------------------|-----|-----|

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## 17. Shareholders' Equity

## Other Comprehensive Income

The following tables present the changes in each component of accumulated other comprehensive income ("AOCI") and the effect of reclassifications out of AOCI on the respective line items in net income.

Changes in Accumulated Other Comprehensive Income by Component  
First Quarter 2016

|                                                            | Net Unrealized<br>Gains (Losses) on<br>Investments with<br>no Other-Than-<br>Temporary<br>Impairment<br>(in millions) | Net Unrealized<br>Gains (Losses) on<br>Investments with<br>Other-Than-<br>Temporary<br>Impairment<br>(in millions) | Cumulative<br>Translation<br>Adjustment | Cash Flow Hedge | Total Accumulated<br>Other<br>Comprehensive<br>Income |
|------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------|-----------------------------------------|-----------------|-------------------------------------------------------|
| Balance, December 31, 2015                                 | \$260                                                                                                                 | \$ (15 )                                                                                                           | \$ (16 )                                | \$ 8            | \$ 237                                                |
| Other comprehensive income (loss) before reclassifications | 95                                                                                                                    | (17 )                                                                                                              | (2 )                                    | —               | 76                                                    |
| Amounts reclassified from AOCI to:                         |                                                                                                                       |                                                                                                                    |                                         |                 |                                                       |
| Net realized investment gains (losses)                     | (4 )                                                                                                                  | 17                                                                                                                 | —                                       | —               | 13                                                    |
| Net investment income                                      | (3 )                                                                                                                  | —                                                                                                                  | —                                       | —               | (3 )                                                  |
| Interest expense                                           | —                                                                                                                     | —                                                                                                                  | —                                       | 0               | 0                                                     |
| Total before tax                                           | (7 )                                                                                                                  | 17                                                                                                                 | —                                       | 0               | 10                                                    |
| Tax (provision) benefit                                    | 2                                                                                                                     | (6 )                                                                                                               | —                                       | 0               | (4 )                                                  |
| Total amount reclassified from AOCI, net of tax            | (5 )                                                                                                                  | 11                                                                                                                 | —                                       | 0               | 6                                                     |
| Net current period other comprehensive income (loss)       | 90                                                                                                                    | (6 )                                                                                                               | (2 )                                    | 0               | 82                                                    |
| Balance, March 31, 2016                                    | \$350                                                                                                                 | \$ (21 )                                                                                                           | \$ (18 )                                | \$ 8            | \$ 319                                                |

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First Quarter 2015

|                                                               | Net Unrealized<br>Gains (Losses) on<br>Investments with<br>no Other-Than-<br>Temporary<br>Impairment<br>(in millions) | Net Unrealized<br>Gains (Losses) on<br>Investments with<br>Other-Than-<br>Temporary<br>Impairment<br>(in millions) | Cumulative<br>Translation<br>Adjustment | Cash Flow<br>Hedge | Total Accumulated<br>Other<br>Comprehensive<br>Income |
|---------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------|-----------------------------------------|--------------------|-------------------------------------------------------|
| Balance, December 31, 2014                                    | \$367                                                                                                                 | \$ 4                                                                                                               | \$ (10 )                                | \$ 9               | \$ 370                                                |
| Other comprehensive income (loss) before<br>reclassifications | 18                                                                                                                    | (2 )                                                                                                               | (5 )                                    | —                  | 11                                                    |
| Amounts reclassified from AOCI to:                            |                                                                                                                       |                                                                                                                    |                                         |                    |                                                       |
| Net realized investment gains (losses)                        | (20 )                                                                                                                 | 4                                                                                                                  | —                                       | —                  | (16 )                                                 |
| Interest expense                                              | —                                                                                                                     | —                                                                                                                  | —                                       | (1 )               | (1 )                                                  |
| Total before tax                                              | (20 )                                                                                                                 | 4                                                                                                                  | —                                       | (1 )               | (17 )                                                 |
| Tax (provision) benefit                                       | 7                                                                                                                     | (1 )                                                                                                               | —                                       | 0                  | 6                                                     |
| Total amount reclassified from AOCI, net of tax               | (13 )                                                                                                                 | 3                                                                                                                  | —                                       | (1 )               | (11 )                                                 |
| Net current period other comprehensive income<br>(loss)       | 5                                                                                                                     | 1                                                                                                                  | (5 )                                    | (1 )               | 0                                                     |
| Balance, March 31, 2015                                       | \$372                                                                                                                 | \$ 5                                                                                                               | \$ (15 )                                | \$ 8               | \$ 370                                                |

## Share Repurchase

The following table presents share repurchases by quarter since January 2013.

## Share Repurchases

| Period                                             | Number of<br>Shares<br>Repurchased | Total<br>Payments(in<br>millions) | Average<br>Price<br>Paid Per<br>Share |
|----------------------------------------------------|------------------------------------|-----------------------------------|---------------------------------------|
| 2013                                               | 12,512,759                         | \$ 264                            | \$ 21.12                              |
| 2014                                               | 24,413,781                         | 590                               | 24.17                                 |
| 2015 (January 1 - March 31)                        | 5,860,291                          | 152                               | 25.87                                 |
| 2015 (April 1 - June 30)                           | 4,737,388                          | 133                               | 28.13                                 |
| 2015 (July 1 - September 30)                       | 5,362,103                          | 135                               | 25.17                                 |
| 2015 (October 1 - December 31)                     | 5,035,637                          | 135                               | 26.81                                 |
| Total 2015                                         | 20,995,419                         | 555                               | 26.43                                 |
| 2016 (January 1 - March 31)                        | 3,038,928                          | 75                                | 24.69                                 |
| 2016 (April 1 - through May 4, 2016)               | 793,672                            | 20                                | 25.20                                 |
| Total 2016                                         | 3,832,600                          | 95                                | 24.80                                 |
| Cumulative repurchases since the beginning of 2013 | 61,754,559                         | \$ 1,504                          | \$ 24.36                              |

On February 24, 2016, the Board of Directors approved a \$250 million share repurchase authorization. The Company expects to repurchase shares from time to time in the open market or in privately negotiated transactions. The timing,

form and amount of the share repurchases under the program are at the discretion of management and will depend on a variety of factors, including funds available at the parent company, market conditions, the Company's capital position, legal requirements and other factors. The repurchase program may be modified, extended or terminated by the Board of Directors at any time. It does not have an expiration date. As of March 31, 2016, the Company's remaining share repurchase authorization was \$230 million, and as of May 4, 2016, it was approximately \$210 million.

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## 18. Subsidiary Information

The following tables present the condensed consolidating financial information for AGUS and AGMH, 100%-owned subsidiaries of AGL, which have issued publicly traded debt securities (see Note 15, Long Term Debt and Credit Facilities). The information for AGL, AGUS and AGMH presents its subsidiaries on the equity method of accounting.

## CONDENSED CONSOLIDATING BALANCE SHEET

AS OF MARCH 31, 2016

(in millions)

|                                                                              | Assured<br>Guaranty Ltd.<br>(Parent) | AGUS<br>(Issuer) | AGMH<br>(Issuer) | Other<br>Entities | Consolidating<br>Adjustments | Assured<br>Guaranty Ltd.<br>(Consolidated) |
|------------------------------------------------------------------------------|--------------------------------------|------------------|------------------|-------------------|------------------------------|--------------------------------------------|
| <b>ASSETS</b>                                                                |                                      |                  |                  |                   |                              |                                            |
| Total investment portfolio and cash                                          | \$ 80                                | \$94             | \$23             | \$11,489          | \$ (360)                     | ) \$ 11,326                                |
| Investment in subsidiaries                                                   | 6,003                                | 5,570            | 4,077            | 389               | (16,039)                     | ) —                                        |
| Premiums receivable, net of commissions payable                              | —                                    | —                | —                | 792               | (130)                        | ) 662                                      |
| Ceded unearned premium reserve                                               | —                                    | —                | —                | 1,236             | (1,000)                      | ) 236                                      |
| Deferred acquisition costs                                                   | —                                    | —                | —                | 172               | (59)                         | ) 113                                      |
| Reinsurance recoverable on unpaid losses                                     | —                                    | —                | —                | 491               | (419)                        | ) 72                                       |
| Credit derivative assets                                                     | —                                    | —                | —                | 163               | (108)                        | ) 55                                       |
| Deferred tax asset, net                                                      | —                                    | 40               | —                | 368               | (130)                        | ) 278                                      |
| Intercompany receivable                                                      | —                                    | —                | —                | 90                | (90)                         | ) —                                        |
| Financial guaranty variable interest entities' assets,<br>at fair value      | —                                    | —                | —                | 1,191             | —                            | ) 1,191                                    |
| Other                                                                        | 34                                   | 46               | 28               | 645               | (234)                        | ) 519                                      |
| <b>TOTAL ASSETS</b>                                                          | <b>\$ 6,117</b>                      | <b>\$5,750</b>   | <b>\$4,128</b>   | <b>\$17,026</b>   | <b>\$ (18,569)</b>           | <b>) \$ 14,452</b>                         |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>                                  |                                      |                  |                  |                   |                              |                                            |
| Unearned premium reserves                                                    | \$ —                                 | \$—              | \$—              | \$4,914           | \$ (1,104)                   | ) \$ 3,810                                 |
| Loss and LAE reserve                                                         | —                                    | —                | —                | 1,605             | (493)                        | ) 1,112                                    |
| Long-term debt                                                               | —                                    | 842              | 447              | 13                | —                            | ) 1,302                                    |
| Intercompany payable                                                         | —                                    | 90               | —                | 300               | (390)                        | ) —                                        |
| Credit derivative liabilities                                                | —                                    | —                | —                | 597               | (108)                        | ) 489                                      |
| Deferred tax liabilities, net                                                | —                                    | —                | 90               | —                 | (90)                         | ) —                                        |
| Financial guaranty variable interest entities'<br>liabilities, at fair value | —                                    | —                | —                | 1,284             | —                            | ) 1,284                                    |
| Other                                                                        | 4                                    | 26               | 18               | 655               | (361)                        | ) 342                                      |
| <b>TOTAL LIABILITIES</b>                                                     | <b>4</b>                             | <b>958</b>       | <b>555</b>       | <b>9,368</b>      | <b>(2,546)</b>               | <b>) 8,339</b>                             |
| <b>TOTAL SHAREHOLDERS' EQUITY</b>                                            |                                      |                  |                  |                   |                              |                                            |
| <b>ATTRIBUTABLE TO ASSURED GUARANTY<br/>LTD.</b>                             | <b>6,113</b>                         | <b>4,792</b>     | <b>3,573</b>     | <b>7,269</b>      | <b>(15,634)</b>              | <b>) 6,113</b>                             |
| Noncontrolling interest                                                      | —                                    | —                | —                | 389               | (389)                        | ) —                                        |
| <b>TOTAL SHAREHOLDERS' EQUITY</b>                                            | <b>6,113</b>                         | <b>4,792</b>     | <b>3,573</b>     | <b>7,658</b>      | <b>(16,023)</b>              | <b>) 6,113</b>                             |
| <b>TOTAL LIABILITIES AND<br/>SHAREHOLDERS' EQUITY</b>                        | <b>\$ 6,117</b>                      | <b>\$5,750</b>   | <b>\$4,128</b>   | <b>\$17,026</b>   | <b>\$ (18,569)</b>           | <b>) \$ 14,452</b>                         |



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## CONDENSED CONSOLIDATING BALANCE SHEET

AS OF DECEMBER 31, 2015

(in millions)

|                                                                           | Assured<br>Guaranty Ltd.<br>(Parent) | AGUS<br>(Issuer) | AGMH<br>(Issuer) | Other<br>Entities | Consolidating<br>Adjustments | Assured<br>Guaranty Ltd.<br>(Consolidated) |
|---------------------------------------------------------------------------|--------------------------------------|------------------|------------------|-------------------|------------------------------|--------------------------------------------|
| <b>ASSETS</b>                                                             |                                      |                  |                  |                   |                              |                                            |
| Total investment portfolio and cash                                       | \$ 10                                | \$ 156           | \$ 22            | \$ 11,530         | \$ (360 )                    | \$ 11,358                                  |
| Investment in subsidiaries                                                | 5,961                                | 5,569            | 4,081            | 377               | (15,988 )                    | —                                          |
| Premiums receivable, net of commissions payable                           | —                                    | —                | —                | 833               | (140 )                       | 693                                        |
| Ceded unearned premium reserve                                            | —                                    | —                | —                | 1,266             | (1,034 )                     | 232                                        |
| Deferred acquisition costs                                                | —                                    | —                | —                | 176               | (62 )                        | 114                                        |
| Reinsurance recoverable on unpaid losses                                  | —                                    | —                | —                | 467               | (398 )                       | 69                                         |
| Credit derivative assets                                                  | —                                    | —                | —                | 207               | (126 )                       | 81                                         |
| Deferred tax asset, net                                                   | —                                    | 52               | —                | 357               | (133 )                       | 276                                        |
| Intercompany receivable                                                   | —                                    | —                | —                | 90                | (90 )                        | —                                          |
| Financial guaranty variable interest entities' assets, at fair value      | —                                    | —                | —                | 1,261             | —                            | 1,261                                      |
| Other                                                                     | 98                                   | 29               | 26               | 571               | (264 )                       | 460                                        |
| <b>TOTAL ASSETS</b>                                                       | <b>\$ 6,069</b>                      | <b>\$ 5,806</b>  | <b>\$ 4,129</b>  | <b>\$ 17,135</b>  | <b>\$ (18,595 )</b>          | <b>\$ 14,544</b>                           |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>                               |                                      |                  |                  |                   |                              |                                            |
| Unearned premium reserves                                                 | \$ —                                 | \$ —             | \$ —             | \$ 5,143          | \$ (1,147 )                  | \$ 3,996                                   |
| Loss and LAE reserve                                                      | —                                    | —                | —                | 1,537             | (470 )                       | 1,067                                      |
| Long-term debt                                                            | —                                    | 842              | 445              | 13                | —                            | 1,300                                      |
| Intercompany payable                                                      | —                                    | 90               | —                | 300               | (390 )                       | —                                          |
| Credit derivative liabilities                                             | —                                    | —                | —                | 572               | (126 )                       | 446                                        |
| Deferred tax liabilities, net                                             | —                                    | —                | 91               | —                 | (91 )                        | —                                          |
| Financial guaranty variable interest entities' liabilities, at fair value | —                                    | —                | —                | 1,349             | —                            | 1,349                                      |
| Other                                                                     | 6                                    | 82               | 15               | 622               | (402 )                       | 323                                        |
| <b>TOTAL LIABILITIES</b>                                                  | <b>6</b>                             | <b>1,014</b>     | <b>551</b>       | <b>9,536</b>      | <b>(2,626 )</b>              | <b>8,481</b>                               |
| <b>TOTAL SHAREHOLDERS' EQUITY</b>                                         |                                      |                  |                  |                   |                              |                                            |
| ATTRIBUTABLE TO ASSURED GUARANTY LTD.                                     | 6,063                                | 4,792            | 3,578            | 7,222             | (15,592 )                    | 6,063                                      |
| Noncontrolling interest                                                   | —                                    | —                | —                | 377               | (377 )                       | —                                          |
| <b>TOTAL SHAREHOLDERS' EQUITY</b>                                         | <b>6,063</b>                         | <b>4,792</b>     | <b>3,578</b>     | <b>7,599</b>      | <b>(15,969 )</b>             | <b>6,063</b>                               |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>                         | <b>\$ 6,069</b>                      | <b>\$ 5,806</b>  | <b>\$ 4,129</b>  | <b>\$ 17,135</b>  | <b>\$ (18,595 )</b>          | <b>\$ 14,544</b>                           |



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CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS  
AND COMPREHENSIVE INCOME  
FOR THE THREE MONTHS ENDED MARCH 31, 2016  
(in millions)

|                                                                                     | Assured<br>Guaranty Ltd.<br>(Parent) | AGUS<br>(Issuer) | AGMH<br>(Issuer) | Other<br>Entities | Consolidating<br>Adjustments | Assured<br>Guaranty Ltd.<br>(Consolidated) |
|-------------------------------------------------------------------------------------|--------------------------------------|------------------|------------------|-------------------|------------------------------|--------------------------------------------|
| <b>REVENUES</b>                                                                     |                                      |                  |                  |                   |                              |                                            |
| Net earned premiums                                                                 | \$ —                                 | \$ —             | \$ —             | \$ 192            | \$ (9 )                      | \$ 183                                     |
| Net investment income                                                               | 0                                    | 0                | 0                | 100               | (1 )                         | 99                                         |
| Net realized investment gains (losses)                                              | 0                                    | —                | —                | (12 )             | (1 )                         | (13 )                                      |
| Net change in fair value of credit derivatives:                                     |                                      |                  |                  |                   |                              |                                            |
| Realized gains (losses) and other settlements                                       | —                                    | —                | —                | 8                 | 0                            | 8                                          |
| Net unrealized gains (losses)                                                       | —                                    | —                | —                | (68 )             | —                            | (68 )                                      |
| Net change in fair value of credit derivatives                                      | —                                    | —                | —                | (60 )             | 0                            | (60 )                                      |
| Bargain purchase gain and settlement of pre-existing relationships                  | —                                    | —                | —                | —                 | —                            | —                                          |
| Other                                                                               | 0                                    | —                | —                | 36                | —                            | 36                                         |
| <b>TOTAL REVENUES</b>                                                               | <b>0</b>                             | <b>0</b>         | <b>0</b>         | <b>256</b>        | <b>(11 )</b>                 | <b>245</b>                                 |
| <b>EXPENSES</b>                                                                     |                                      |                  |                  |                   |                              |                                            |
| Loss and LAE                                                                        | —                                    | —                | —                | 93                | (3 )                         | 90                                         |
| Amortization of deferred acquisition costs                                          | —                                    | —                | —                | 7                 | (3 )                         | 4                                          |
| Interest expense                                                                    | —                                    | 13               | 13               | 3                 | (3 )                         | 26                                         |
| Other operating expenses                                                            | 8                                    | 0                | 1                | 52                | (1 )                         | 60                                         |
| <b>TOTAL EXPENSES</b>                                                               | <b>8</b>                             | <b>13</b>        | <b>14</b>        | <b>155</b>        | <b>(10 )</b>                 | <b>180</b>                                 |
| <b>INCOME (LOSS) BEFORE INCOME TAXES AND EQUITY IN NET EARNINGS OF SUBSIDIARIES</b> | <b>(8 )</b>                          | <b>(13 )</b>     | <b>(14 )</b>     | <b>101</b>        | <b>(1 )</b>                  | <b>65</b>                                  |
| Total (provision) benefit for income taxes                                          | —                                    | 5                | 5                | (16 )             | 0                            | (6 )                                       |
| Equity in net earnings of subsidiaries                                              | 67                                   | 50               | 77               | 9                 | (203 )                       | —                                          |
| <b>NET INCOME (LOSS)</b>                                                            | <b>\$ 59</b>                         | <b>\$ 42</b>     | <b>\$ 68</b>     | <b>\$ 94</b>      | <b>\$ (204 )</b>             | <b>\$ 59</b>                               |
| Less: noncontrolling interest                                                       | —                                    | —                | —                | 9                 | (9 )                         | —                                          |
| <b>NET INCOME (LOSS) ATTRIBUTABLE TO ASSURED GUARANTY LTD.</b>                      | <b>\$ 59</b>                         | <b>\$ 42</b>     | <b>\$ 68</b>     | <b>\$ 85</b>      | <b>\$ (195 )</b>             | <b>\$ 59</b>                               |
| <br><b>COMPREHENSIVE INCOME (LOSS)</b>                                              | <br><b>\$ 141</b>                    | <br><b>\$ 80</b> | <br><b>\$ 92</b> | <br><b>\$ 178</b> | <br><b>\$ (350 )</b>         | <br><b>\$ 141</b>                          |

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CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS  
AND COMPREHENSIVE INCOME  
FOR THE THREE MONTHS ENDED MARCH 31, 2015  
(in millions)

|                                                                                         | Assured<br>Guaranty Ltd.<br>(Parent) | AGUS<br>(Issuer)  | AGMH<br>(Issuer) | Other<br>Entities | Consolidating<br>Adjustments | Assured<br>Guaranty Ltd.<br>(Consolidated) |
|-----------------------------------------------------------------------------------------|--------------------------------------|-------------------|------------------|-------------------|------------------------------|--------------------------------------------|
| <b>REVENUES</b>                                                                         |                                      |                   |                  |                   |                              |                                            |
| Net earned premiums                                                                     | \$ —                                 | \$ —              | \$ —             | \$ 140            | \$ 2                         | \$ 142                                     |
| Net investment income                                                                   | 0                                    | 0                 | 0                | 104               | (3)                          | 101                                        |
| Net realized investment gains (losses)                                                  | 0                                    | 0                 | 0                | 19                | (3)                          | 16                                         |
| Net change in fair value of credit derivatives:                                         |                                      |                   |                  |                   |                              |                                            |
| Realized gains (losses) and other settlements                                           | —                                    | —                 | —                | 21                | 0                            | 21                                         |
| Net unrealized gains (losses)                                                           | —                                    | —                 | —                | 103               | —                            | 103                                        |
| Net change in fair value of credit derivatives                                          | —                                    | —                 | —                | 124               | 0                            | 124                                        |
| Other                                                                                   | —                                    | —                 | —                | (14)              | —                            | (14)                                       |
| <b>TOTAL REVENUES</b>                                                                   | <b>0</b>                             | <b>0</b>          | <b>0</b>         | <b>373</b>        | <b>(4)</b>                   | <b>369</b>                                 |
| <b>EXPENSES</b>                                                                         |                                      |                   |                  |                   |                              |                                            |
| Loss and LAE                                                                            | —                                    | —                 | —                | 18                | 0                            | 18                                         |
| Amortization of deferred acquisition costs                                              | —                                    | —                 | —                | 6                 | (2)                          | 4                                          |
| Interest expense                                                                        | —                                    | 13                | 13               | 4                 | (5)                          | 25                                         |
| Other operating expenses                                                                | 8                                    | 0                 | 0                | 48                | 0                            | 56                                         |
| <b>TOTAL EXPENSES</b>                                                                   | <b>8</b>                             | <b>13</b>         | <b>13</b>        | <b>76</b>         | <b>(7)</b>                   | <b>103</b>                                 |
| <b>INCOME (LOSS) BEFORE INCOME TAXES AND<br/>EQUITY IN NET EARNINGS OF SUBSIDIARIES</b> | <b>(8)</b>                           | <b>(13)</b>       | <b>(13)</b>      | <b>297</b>        | <b>3</b>                     | <b>266</b>                                 |
| Total (provision) benefit for income taxes                                              | —                                    | 5                 | 5                | (72)              | (3)                          | (65)                                       |
| Equity in net earnings of subsidiaries                                                  | 209                                  | 163               | 92               | 9                 | (473)                        | —                                          |
| <b>NET INCOME (LOSS)</b>                                                                | <b>\$ 201</b>                        | <b>\$ 155</b>     | <b>\$ 84</b>     | <b>\$ 234</b>     | <b>\$ (473)</b>              | <b>\$ 201</b>                              |
| Less: noncontrolling interest                                                           | —                                    | —                 | —                | 9                 | (9)                          | —                                          |
| <b>NET INCOME (LOSS) ATTRIBUTABLE TO<br/>ASSURED GUARANTY LTD.</b>                      | <b>\$ 201</b>                        | <b>\$ 155</b>     | <b>\$ 84</b>     | <b>\$ 225</b>     | <b>\$ (464)</b>              | <b>\$ 201</b>                              |
| <br><b>COMPREHENSIVE INCOME (LOSS)</b>                                                  | <br><b>\$ 201</b>                    | <br><b>\$ 134</b> | <br><b>\$ 80</b> | <br><b>\$ 233</b> | <br><b>\$ (447)</b>          | <br><b>\$ 201</b>                          |

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CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS  
FOR THE THREE MONTHS ENDED MARCH 31, 2016  
(in millions)

|                                                                   | Assured<br>Guaranty Ltd.<br>(Parent) | AGUS<br>(Issuer) | AGMH<br>(Issuer) | Other<br>Entities | Consolidating<br>Adjustments | Assured<br>Guaranty Ltd.<br>(Consolidated) |
|-------------------------------------------------------------------|--------------------------------------|------------------|------------------|-------------------|------------------------------|--------------------------------------------|
| Net cash flows provided by (used in) operating activities         | \$ 166                               | \$ 17            | \$ 88            | \$ (74 )          | \$ (287 )                    | \$ (90 )                                   |
| Cash flows from investing activities                              |                                      |                  |                  |                   |                              |                                            |
| Fixed-maturity securities:                                        |                                      |                  |                  |                   |                              |                                            |
| Purchases                                                         | (4 )                                 | (11 )            | —                | (281 )            | —                            | (296 )                                     |
| Sales                                                             | 1                                    | —                | —                | 161               | —                            | 162                                        |
| Maturities                                                        | —                                    | —                | —                | 301               | —                            | 301                                        |
| Sales (purchases) of short-term investments, net                  | (69 )                                | 11               | —                | (5 )              | —                            | (63 )                                      |
| Net proceeds from financial guaranty variable entities' assets    | —                                    | —                | —                | 66                | —                            | 66                                         |
| Intercompany debt                                                 | —                                    | —                | —                | —                 | —                            | —                                          |
| Investment in subsidiary                                          | —                                    | —                | —                | —                 | —                            | —                                          |
| Other                                                             | —                                    | —                | —                | 2                 | —                            | 2                                          |
| Net cash flows provided by (used in) investing activities         | (72 )                                | 0                | —                | 244               | —                            | 172                                        |
| Cash flows from financing activities                              |                                      |                  |                  |                   |                              |                                            |
| Return of capital                                                 | —                                    | —                | —                | —                 | —                            | —                                          |
| Dividends paid                                                    | (18 )                                | (80 )            | (87 )            | (120 )            | 287                          | (18 )                                      |
| Repurchases of common stock                                       | (75 )                                | —                | —                | —                 | —                            | (75 )                                      |
| Share activity under option and incentive plans                   | 0                                    | —                | —                | —                 | —                            | 0                                          |
| Net paydowns of financial guaranty variable entities' liabilities | —                                    | —                | —                | (42 )             | —                            | (42 )                                      |
| Payment of long-term debt                                         | —                                    | —                | —                | 0                 | —                            | 0                                          |
| Intercompany debt                                                 | —                                    | —                | —                | —                 | —                            | —                                          |
| Other                                                             | —                                    | —                | —                | (1 )              | —                            | (1 )                                       |
| Net cash flows provided by (used in) financing activities         | (93 )                                | (80 )            | (87 )            | (163 )            | 287                          | (136 )                                     |
| Effect of exchange rate changes                                   | —                                    | —                | —                | 0                 | —                            | 0                                          |
| Increase (decrease) in cash                                       | 1                                    | (63 )            | 1                | 7                 | —                            | (54 )                                      |
| Cash at beginning of period                                       | 0                                    | 95               | 8                | 63                | —                            | 166                                        |
| Cash at end of period                                             | \$ 1                                 | \$ 32            | \$ 9             | \$ 70             | \$ —                         | \$ 112                                     |

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CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS  
FOR THE THREE MONTHS ENDED MARCH 31, 2015  
(in millions)

|                                                                   | Assured<br>Guaranty Ltd.<br>(Parent) | AGUS<br>(Issuer) | AGMH<br>(Issuer) | Other<br>Entities | Consolidating<br>Adjustments | Assured<br>Guaranty Ltd.<br>(Consolidated) |
|-------------------------------------------------------------------|--------------------------------------|------------------|------------------|-------------------|------------------------------|--------------------------------------------|
| Net cash flows provided by (used in) operating activities         | \$ 97                                | \$ 127           | \$ 59            | \$ 34             | \$ (294 )                    | \$ 23                                      |
| Cash flows from investing activities                              |                                      |                  |                  |                   |                              |                                            |
| Fixed-maturity securities:                                        |                                      |                  |                  |                   |                              |                                            |
| Purchases                                                         | —                                    | (46 )            | (6 )             | (396 )            | —                            | (448 )                                     |
| Sales                                                             | —                                    | 122              | 11               | 708               | —                            | 841                                        |
| Maturities                                                        | —                                    | 4                | —                | 151               | —                            | 155                                        |
| Sales (purchases) of short-term investments, net                  | 79                                   | 43               | 19               | 279               | —                            | 420                                        |
| Net proceeds from financial guaranty variable entities' assets    | —                                    | —                | —                | 30                | —                            | 30                                         |
| Intercompany debt                                                 | —                                    | (200 )           | —                | —                 | 200                          | —                                          |
| Investment in subsidiary                                          | —                                    | —                | 25               | —                 | (25 )                        | —                                          |
| Other                                                             | —                                    | —                | —                | 3                 | —                            | 3                                          |
| Net cash flows provided by (used in) investing activities         | 79                                   | (77 )            | 49               | 775               | 175                          | 1,001                                      |
| Cash flows from financing activities                              |                                      |                  |                  |                   |                              |                                            |
| Return of capital                                                 | —                                    | —                | —                | (25 )             | 25                           | —                                          |
| Dividends paid                                                    | (19 )                                | (50 )            | (108 )           | (136 )            | 294                          | (19 )                                      |
| Repurchases of common stock                                       | (152 )                               | —                | —                | —                 | —                            | (152 )                                     |
| Share activity under option and incentive plans                   | (5 )                                 | —                | —                | —                 | —                            | (5 )                                       |
| Net paydowns of financial guaranty variable entities' liabilities | —                                    | —                | —                | (39 )             | —                            | (39 )                                      |
| Payment of long-term debt                                         | —                                    | —                | —                | (1 )              | —                            | (1 )                                       |
| Intercompany debt                                                 | —                                    | —                | —                | 200               | (200 )                       | —                                          |
| Other                                                             | —                                    | —                | —                | 4                 | —                            | 4                                          |
| Net cash flows provided by (used in) financing activities         | (176 )                               | (50 )            | (108 )           | 3                 | 119                          | (212 )                                     |
| Effect of exchange rate changes                                   | —                                    | —                | —                | (2 )              | —                            | (2 )                                       |
| Increase (decrease) in cash                                       | —                                    | —                | —                | 810               | —                            | 810                                        |
| Cash at beginning of period                                       | 0                                    | —                | 4                | 71                | —                            | 75                                         |
| Cash at end of period                                             | \$ 0                                 | \$ —             | \$ 4             | \$ 881            | \$ —                         | \$ 885                                     |

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ITEM MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
2. OPERATIONS  
Forward Looking Statements

This Form 10-Q contains information that includes or is based upon forward looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward looking statements give the expectations or forecasts of future events of Assured Guaranty Ltd. ("AGL") and its subsidiaries (collectively with AGL, "Assured Guaranty" or the "Company"). These statements can be identified by the fact that they do not relate strictly to historical or current facts and relate to future operating or financial performance.

Any or all of Assured Guaranty's forward looking statements herein are based on current expectations and the current economic environment and may turn out to be incorrect. Assured Guaranty's actual results may vary materially. Among factors that could cause actual results to differ adversely are:

- rating agency action, including a ratings downgrade, a change in outlook, the placement of ratings on watch for downgrade, or a change in rating criteria, at any time, of AGL or any of its subsidiaries, and/or of any securities AGL or any of its subsidiaries have issued, and/or of transactions that AGL's subsidiaries have insured;
- reduction in the amount of available insurance opportunities and/or in the demand for Assured Guaranty's insurance;
- developments in the world's financial and capital markets that adversely affect obligors' payment rates, Assured Guaranty's loss experience, or its exposure to refinancing risk in transactions (which could result in substantial liquidity claims on its guarantees);
- the possibility that budget or pension shortfalls or other factors will result in credit losses or impairments on obligations of state, territorial and local governments and their related authorities and public corporations that Assured Guaranty insures or reinsures;
- the failure of Assured Guaranty to realize loss recoveries that are assumed in its expected loss estimates;
- deterioration in the financial condition of Assured Guaranty's reinsurers, the amount and timing of reinsurance recoverables actually received and the risk that reinsurers may dispute amounts owed to Assured Guaranty under its reinsurance agreements;
- increased competition, including from new entrants into the financial guaranty industry;
- rating agency action on obligors, including sovereign debtors, resulting in a reduction in the value of securities in Assured Guaranty's investment portfolio and in collateral posted by and to Assured Guaranty;
- the inability of Assured Guaranty to access external sources of capital on acceptable terms;
- changes in the world's credit markets, segments thereof, interest rates or general economic conditions;
- the impact of market volatility on the mark-to-market of Assured Guaranty's contracts written in credit default swap form;
- changes in applicable accounting policies or practices;
- changes in applicable laws or regulations, including insurance, bankruptcy and tax laws, or other governmental actions;
- difficulties with the execution of Assured Guaranty's business strategy;
- loss of key personnel;
- the effects of mergers, acquisitions and divestitures;
- natural or man-made catastrophes;
- other risks and uncertainties that have not been identified at this time;

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management's response to these factors; and

other risk factors identified in AGL's filings with the U.S. Securities and Exchange Commission (the "SEC").

The foregoing review of important factors should not be construed as exhaustive, and should be read in conjunction with the other cautionary statements that are included in this Form 10-Q, as well as the risk factors included in AGL's 2015 Annual Report on Form 10-K. The Company undertakes no obligation to update publicly or review any forward looking statement, whether as a result of new information, future developments or otherwise, except as required by law. Investors are advised, however, to consult any further disclosures the Company makes on related subjects in the Company's reports filed with the SEC.

If one or more of these or other risks or uncertainties materialize, or if the Company's underlying assumptions prove to be incorrect, actual results may vary materially from what the Company projected. Any forward looking statements in this Form 10-Q reflect the Company's current views with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to its operations, results of operations, growth strategy and liquidity.

For these statements, the Company claims the protection of the safe harbor for forward looking statements contained in Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act").

## Available Information

The Company maintains an Internet web site at [www.assuredguaranty.com](http://www.assuredguaranty.com). The Company makes available, free of charge, on its web site (under [assuredguaranty.com/sec-filings](http://assuredguaranty.com/sec-filings)) the Company's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13 (a) or 15 (d) of the Exchange Act as soon as reasonably practicable after the Company files such material with, or furnishes it to, the SEC. The Company also makes available, free of charge, through its web site (under [assuredguaranty.com/governance](http://assuredguaranty.com/governance)) links to the Company's Corporate Governance Guidelines, its Code of Conduct, AGL's Bye-Laws and the charters for its Board committees.

The Company routinely posts important information for investors on its web site (under [assuredguaranty.com/company-statements](http://assuredguaranty.com/company-statements) and, more generally, under the Investor Information and Businesses pages). The Company uses this web site as a means of disclosing material information and for complying with its disclosure obligations under SEC Regulation FD (Fair Disclosure). Accordingly, investors should monitor the Company Statements, Investor Information and Businesses portions of the Company's web site, in addition to following the Company's press releases, SEC filings, public conference calls, presentations and webcasts.

The information contained on, or that may be accessed through, the Company's web site is not incorporated by reference into, and is not a part of, this report.

## Executive Summary

This executive summary of management's discussion and analysis highlights selected information and may not contain all of the information that is important to readers of this Quarterly Report. For a more detailed description of events, trends and uncertainties, as well as the capital, liquidity, credit, operational and market risks and the critical accounting policies and estimates affecting the Company, this Quarterly Report should be read in its entirety and in addition to AGL's 2015 Annual Report on Form 10-K.

## Economic Environment



The amount and pricing of new business the Company originates as well as the financial health of the issuers whose obligations it insures depends in part on the economic environment in the markets it serves, including the level of interest rates and credit spreads in those markets.

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The overall economic environment in the United States ("U.S.") continued improving during the three-month period ended March 31, 2016 ("First Quarter 2016"). The U.S. Department of Commerce Bureau of Economic Analysis reported that gross domestic product increased at an annual rate of 0.5% in First Quarter 2016. According to the U.S. Bureau of Labor Statistics ("BLS"), the estimated unemployment rate fell to 4.9% in January and February, the lowest monthly level since April 2008, and rose slightly to 5.0% in March. The BLS also reported that the U.S. economy added more than 430,000 jobs during the first three months of 2016, a 2% increase over the comparable prior-year period. U.S. home prices, as measured by the Case-Shiller Index, continued to rise across the country over the last 12 months, although the pace of growth has slowed year-over-year.

The Federal Open Market Committee ("FOMC") position has maintained the target range for the federal funds rate at 1/4 to 1/2 percent and continues to support further improvement in labor market conditions and a return to 2% inflation. The U.S. stock market opened the new year in decline, with some commentators attributing the decline to global economic uncertainty and weak oil prices that threatened certain U.S. companies. The U.S. stock market rose in February after the Federal Reserve board chair indicated in Congressional testimony that further increases in the federal funds rate would be gradual, and as oil prices began to recover. Average municipal interest rates in First Quarter 2016 were similar to those of first quarter 2015 and 25 basis points lower than the full-year average for 2015, based on the 30-year AAA MMD Index.

The European Central Bank continued its program of quantitative easing during First Quarter 2016 and started to expand monthly purchases under the asset purchase program to €80 billion on April 1. Interest rates for European bank deposits remain at 0%.

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## Financial Performance of Assured Guaranty

## Financial Results

|                                                  | First<br>Quarter<br>2016 | 2015  |
|--------------------------------------------------|--------------------------|-------|
|                                                  | (in<br>millions)         |       |
| Net income (loss)                                | \$59                     | \$201 |
| Operating income(1)                              | 113                      | 140   |
| Net income (loss) per diluted share              | 0.43                     | 1.28  |
| Operating income per share(1)                    | 0.82                     | 0.89  |
| Diluted shares                                   | 137.0                    | 156.8 |
| Present value of new business production ("PVP") | (1)\$38                  | \$36  |
| Gross par written                                | 2,749                    | 2,708 |

|                                   | As of March<br>31, 2016                    |              | As of<br>December 31,<br>2015 |              |
|-----------------------------------|--------------------------------------------|--------------|-------------------------------|--------------|
|                                   | Amount                                     | Per<br>Share | Amount                        | Per<br>Share |
|                                   | (in millions, except per share<br>amounts) |              |                               |              |
| Shareholders' equity              | \$6,113                                    | \$45.26      | \$6,063                       | \$43.96      |
| Operating shareholders' equity(1) | 5,954                                      | 44.08        | 5,946                         | 43.11        |
| Adjusted book value(1)            | 8,294                                      | 61.40        | 8,439                         | 61.18        |
| Common shares outstanding (2)     | 135.1                                      |              | 137.9                         |              |

Please refer to "—Non-GAAP Financial Measures" for a definition of the financial measures that were not determined (1) in accordance with accounting principles generally accepted in the United States of America ("GAAP") and a reconciliation of the non-GAAP financial measure to the most directly comparable GAAP measure, if available.

(2) Please refer to "Key Business Strategies – Capital Management" below for information on common share repurchases.

## First Quarter 2016

There are several primary drivers of volatility in net income or loss that are not necessarily indicative of credit impairment or improvement, or ultimate economic gains or losses: changes in credit spreads of insured credit derivative obligations; changes in fair value of assets and liabilities of financial guaranty variable interest entities ("FG VIEs") and committed capital securities ("CCS"); changes in the Company's own credit spreads; and changes in risk-free rates used to discount expected losses. Changes in credit spreads generally have the most significant effect on the fair value of credit derivatives and FG VIE assets and liabilities. In addition to non-economic factors, other factors such as: changes in expected losses, the amount and timing of refunding transactions and terminations, realized gains and losses on the investment portfolio (including other-than-temporary impairments), the effects of large settlements and transactions, acquisitions, and the effects of the Company's various loss mitigation strategies, among others, may

also have a significant effect on reported net income or loss in a given reporting period.

Net income for First Quarter 2016 was \$59 million compared with \$201 million in the three-month period ended March 31, 2015 ("First Quarter 2015"). The decrease was due primarily attributable to fair value losses on credit derivatives in First Quarter 2016 compared with gains in First Quarter 2015, higher loss and loss adjustment expenses ("LAE") attributable mainly to Puerto Rico, partially offset by higher net earned premiums due to refundings and terminations and a benefit due to loss mitigation recoveries recorded in other income. The fair value losses on credit derivatives were primarily due to the decreased cost to purchase protection on Assured Guaranty Corp. ("AGC") and Assured Guaranty Municipal Corp. ("AGM").

Non-GAAP operating income in First Quarter 2016 was \$113 million, compared with \$140 million in First Quarter 2015. The decrease in operating income was primarily due to higher expected losses on certain Puerto Rico exposures, partially offset by higher net earned premiums due to refundings and terminations and a benefit due to loss mitigation recoveries recorded in other income.

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## Key Business Strategies

The Company continually evaluates its business strategies. Currently, the Company is pursuing the following business strategies, each described in more detail below:

- New business production
- Capital management
- Alternative strategies to create value, including through acquisitions and commutations
- Loss mitigation

## New Business Production

The Company believes high-profile defaults by municipal obligors, such as Detroit, Michigan and Stockton, California, both of which filed for protection under chapter 9 of the U.S. Bankruptcy Code, and the deteriorating financial condition of Puerto Rico, have led to increased awareness of the value of bond insurance and stimulated demand for the product. The Company believes there will be continued demand for its insurance in this market because, for those exposures that the Company guarantees, it undertakes the tasks of credit selection, analysis, negotiation of terms, surveillance and, if necessary, loss mitigation. The Company believes that its insurance:

- encourages retail investors, who typically have fewer resources than the Company for analyzing municipal bonds, to purchase such bonds;
- enables institutional investors to operate more efficiently; and
- allows smaller, less well-known issuers to gain market access on a more cost-effective basis.

On the other hand, the persistently low interest rate environment continues to dampen demand for bond insurance and, after a number of years in which the Company was essentially the only financial guarantor, there are now two other financial guarantors active in one of its markets.

## U.S. Municipal Market Data

## Based on Sale Date

|                             | First Quarter<br>2016                          |                     | First Quarter 2015 |                     | Year Ended<br>December 31,<br>2015 |                     |
|-----------------------------|------------------------------------------------|---------------------|--------------------|---------------------|------------------------------------|---------------------|
|                             | Par                                            | Number of<br>issues | Par                | Number of<br>issues | Par                                | Number of<br>issues |
|                             | (dollars in billions, except number of issues) |                     |                    |                     |                                    |                     |
| New municipal bonds issued  | \$96.5                                         | 2,787               | \$103.9            | 3,057               | \$377.6                            | 12,076              |
| Total insured               | 5.7                                            | 430                 | 6.0                | 517                 | 25.2                               | 1,880               |
| Insured by Assured Guaranty | 3.0                                            | 198                 | 3.4                | 276                 | 15.1                               | 1,009               |

## Industry Penetration Rates

## U.S. Municipal Market

|                        | First Quarter |      | Year Ended           |
|------------------------|---------------|------|----------------------|
|                        | 2016          | 2015 | December 31,<br>2015 |
| Market penetration par | 5.9%          | 5.7% | 6.7%                 |

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|                                               |      |      |      |
|-----------------------------------------------|------|------|------|
| Market penetration based on number of issues  | 15.4 | 16.9 | 15.6 |
| % of single A par sold                        | 28.0 | 21.6 | 22.1 |
| % of single A transactions sold               | 58.7 | 55.2 | 54.1 |
| % of \$25 million and under par sold          | 17.7 | 19.8 | 18.7 |
| % of \$25 million and under transactions sold | 17.7 | 19.8 | 17.6 |

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## New Business Production

|                             | First Quarter |         |
|-----------------------------|---------------|---------|
|                             | 2016          | 2015    |
|                             | (in millions) |         |
| PVP (1):                    |               |         |
| Public Finance—U.S.         | \$31          | \$13    |
| Public Finance—non-U.S.     | 7             | —       |
| Structured Finance—U.S.     | —             | 18      |
| Structured Finance—non-U.S. | 5             | —       |
| Total PVP                   | \$38          | \$36    |
| Gross Par Written:          |               |         |
| Public Finance—U.S.         | \$2,749       | \$2,441 |
| Public Finance—non-U.S.     | —             | —       |
| Structured Finance—U.S.     | —             | 261     |
| Structured Finance—non-U.S. | 6             | —       |
| Total gross par written     | \$2,749       | \$2,708 |

(1) PVP and Gross Par Written in the table above are based on "close date," when the transaction settles. See "— Non-GAAP Financial Measures – PVP or Present Value of New Business Production."

U.S. public finance PVP increased to \$31 million in First Quarter 2016 from \$13 million in First Quarter 2015 representing an increase of 138%. The average premium rate increased compared with First Quarter 2015 while the average rating of par written remained in the A- category. During First Quarter 2016, Assured Guaranty once again guaranteed the majority of insured par issued.

Non-U.S. public finance PVP in First Quarter 2016 represents additional future premiums related to the restructuring of an existing insured obligation.

Outside the U.S., the Company believes the United Kingdom ("U.K.") currently presents the most new business opportunities for financial guarantees of infrastructure financings, which have typically required such guarantees for capital market access. These transactions typically have long lead times. Assured Guaranty believes it is the only company in the private sector offering such financial guarantees outside the United States.

In general, the Company expects that structured finance opportunities will increase in the future as the global economy recovers, interest rates rise, more issuers return to the capital markets for financings and institutional investors again utilize financial guaranties. The Company considers its involvement in both structured finance and international infrastructure transactions to be beneficial because such transactions diversify both the Company's business opportunities and its risk profile beyond public finance.

## Capital Management

In recent years, the Company has developed strategies to manage capital within the Assured Guaranty group more efficiently.

In February 2016, the Company exhausted its previous \$400 million common share repurchase authorization and on February 24, 2016, the Board of Directors approved an incremental \$250 million share repurchase authorization. The Company expects the repurchases to be made from time to time in the open market or in privately negotiated transactions. The timing, form and amount of the share repurchases under the program are at the discretion of management and will depend on a variety of factors, including free funds available at the parent company, market

conditions, the Company's capital position, legal requirements and other factors. The repurchase program may be modified, extended or terminated by the Board of Directors at any time. It does not have an expiration date. See Note 17, Shareholders' Equity, of the Financial Statements, for additional information about the Company's repurchases of its common shares.

In First Quarter 2016, the Company repurchased a total of 3.0 million common shares for approximately \$75 million at an average price of \$24.69 per share.



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## Summary of Share Repurchases

|                                                    | Amount of                            | Number of Shares | Average price per share |
|----------------------------------------------------|--------------------------------------|------------------|-------------------------|
|                                                    | (in millions, except per share data) |                  |                         |
| 2013                                               | \$264                                | 12.5             | \$ 21.12                |
| 2014                                               | 590                                  | 24.4             | 24.17                   |
| 2015                                               | 555                                  | 21.0             | 26.43                   |
| 2016 (through May 4, 2016)                         | 95                                   | 3.8              | 24.80                   |
| Cumulative repurchases since the beginning of 2013 | \$1,504                              | 61.7             | 24.36                   |

## Accretive Effect of Cumulative Repurchases(1)

|                                | First Quarter |        | As of March 31, 2016 | As of December 31, 2015 |
|--------------------------------|---------------|--------|----------------------|-------------------------|
|                                | 2016          | 2015   |                      |                         |
|                                | (per share)   |        |                      |                         |
| Net income                     | \$0.08        | \$0.25 |                      |                         |
| Operating income               | 0.20          | 0.18   |                      |                         |
| Shareholders' equity           |               |        | \$ 6.43              | \$ 5.75                 |
| Operating shareholders' equity |               |        | 6.07                 | 5.49                    |
| Adjusted book value            |               |        | 11.45                | 10.83                   |

(1) Cumulative repurchases since the beginning of 2013.

As of May 4, 2016, \$210 million of total capacity remained from the authorization, on a settlement basis.

In order to reduce leverage, and possibly rating agency capital charges, the Company has mutually agreed with beneficiaries to terminate selected financial guaranty insurance and credit derivative contracts. In particular, the Company has targeted investment grade securities for which claims are not expected but which carry a disproportionately large rating agency capital charge. The Company terminated investment grade securities of \$1.9 billion and \$0.1 billion in net par in First Quarter 2016 and First Quarter 2015, respectively, of financial guaranty and credit default swap ("CDS") contracts.

## Alternative Strategies

The Company considers alternative strategies in order to create long-term shareholder value. For example, the Company considers opportunities to acquire financial guaranty portfolios, whether by acquiring financial guarantors who are no longer actively writing new business or their insured portfolios, or by commuting business that it had previously ceded. These transactions enable the Company to improve its future earnings and deploy some of its excess capital.

On April 12, 2016, AGC entered into an agreement and plan of merger to acquire CIFG Holding Inc. ("CIFG"), the parent of financial guaranty insurer CIFG Assurance North America, Inc. ("CIFG NA"). AGC expects to pay \$450 million in cash to acquire CIFG, subject to adjustments as contemplated in the agreement, and the acquisition is expected to be completed mid-2016, subject to receipt of anti-trust and insurance regulatory approvals as well as satisfaction of customary closing conditions. CIFG's stockholders have already approved the acquisition. As part of the transaction, CIFG NA will merge into AGC, which will be the surviving entity. As of December 31, 2015, CIFG had a consolidated insured portfolio of \$5.6 billion of net par and approximately \$637 million of consolidated qualified statutory capital.

On April 1, 2015 (the "Acquisition Date"), AGC completed the acquisition of Radian Asset Acquisition for a cash purchase price of \$804.5 million. In connection with the acquisition, AGC acquired Radian Asset's entire insured portfolio, which resulted in an increase in net par outstanding as of the Acquisition Date of approximately \$13.6 billion, consisting of \$9.4 billion public finance net par outstanding and \$4.2 billion structured finance net par outstanding. In 2015, the acquisition contributed net income of approximately \$2.46 per share and operating income of approximately \$2.13 per share, including the bargain purchase gain,

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settlement of pre-existing relationships and activity since the Acquisition Date. Shareholders' equity benefited by \$1.04 per share, operating shareholders' equity benefited by \$1.26 per share and adjusted book value benefited by \$3.73 per share as of the Acquisition Date.

### Loss Mitigation

In an effort to avoid or reduce potential losses in its insurance portfolios, the Company employs a number of strategies.

In the public finance area, the Company believes that its experience and the resources it is prepared to deploy, as well as its ability to provide bond insurance or other contributions as part of a solution, has resulted in more favorable outcomes in distressed public finance situations than would have been the case without its participation, as illustrated, for example, by the Company's role in the Detroit, Michigan; Stockton, California; and Jefferson County, Alabama financial crises. Currently, the Company is an active participant in discussions with the Commonwealth of Puerto Rico and its advisors with respect to a number of Puerto Rico credits. For example, on December 24, 2015, AGC and AGM entered into a Restructuring Support Agreement ("RSA") with Puerto Rico Electric Power Authority ("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. Legislation meeting the requirements of the RSA was enacted on February 16, 2016. The closing of the restructuring transaction, the issuance of the surety bonds and the closing of the bridge financing are subject to certain conditions, including confirmation that the enacted legislation meets all requirements of the RSA and execution of acceptable documentation and legal opinions. 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 restructuring of the insured PREPA revenue bonds, will be implemented. In addition, there also can be no assurance that the negotiations with respect to other Puerto Rico credits will result in agreements on a consensual recovery plans.

The Company is currently working with the servicers of some of the residential mortgage-backed securities ("RMBS") it insures to encourage the servicers to provide alternatives to distressed borrowers that will encourage them to continue making payments on their loans and so improve the performance of the related RMBS. Many of the HELOC loans underlying the HELOC RMBS are entering their amortization periods, which results in material increases to the size of the monthly payments the borrowers are required to make.

The Company also continues to purchase attractively priced obligations, including below-investment-grade ("BIG") obligations, 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"). These purchases resulted in a reduction of net expected loss to be paid of \$584 million as of March 31, 2016. The fair value of assets purchased for loss mitigation purposes as of March 31, 2016 (excluding the value of the Company's insurance) was \$986 million, with a par of \$1,862 million (including bonds related to FG VIEs of \$153 million in fair value and \$286 million in par).

In some instances, the terms of the Company's policy gives it the option to pay principal on an accelerated basis, thereby reducing the amount of guaranteed interest due in the future. The Company has at times exercised this option, which uses cash but reduces projected future losses.

In an effort to recover losses the Company experienced in its insured U.S. RMBS portfolio, the Company also pursued providers of representations and warranties ("R&W") by enforcing R&W provisions in contracts, negotiating agreements with R&W providers relating to those provisions and, where appropriate, initiating litigation against R&W providers. While the Company has completed its pursuit of R&W claims, it continues to benefit from the agreements reached. See Note 5, Expected Loss to be Paid, of the Financial Statements.

## Results of Operations

### Estimates and Assumptions

The Company's consolidated financial statements include amounts that are determined using estimates and assumptions. The actual amounts realized could ultimately be materially different from the amounts currently provided for in the Company's consolidated financial statements. Management believes the most significant items requiring inherently subjective and complex estimates are expected losses, fair value estimates, other-than-temporary impairment, deferred income taxes, and premium revenue recognition. The following discussion of the results of operations includes information regarding the estimates and assumptions used for these items and should be read in conjunction with the notes to the Company's consolidated financial statements.

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An understanding of the Company's accounting policies is of critical importance to understanding its consolidated financial statements. See Part II, Item 8. "Financial Statements and Supplementary Data" of the Company's Annual Report on Form 10-K for a discussion of significant accounting policies, loss estimation process, approach to projecting U.S. RMBS, and fair value methodologies.

The Company carries a portion of its assets and liabilities at fair value, the majority of which are measured at fair value on a recurring basis. Level 3 assets, consisting primarily of financial guaranty variable interest entities' assets, credit derivative assets, and investments, represented approximately 19% and 20% of total assets measured at fair value on a recurring basis as of March 31, 2016 and December 31, 2015, respectively. All of the Company's liabilities that are measured at fair value are Level 3. See Note 7, Fair Value Measurement, of the Financial Statements for additional information about assets and liabilities classified as Level 3.

## Consolidated Results of Operations

## Consolidated Results of Operations

|                                                 | Three<br>Months<br>Ended March<br>31,<br>2016 2015<br>(in millions) |       |
|-------------------------------------------------|---------------------------------------------------------------------|-------|
| Revenues:                                       |                                                                     |       |
| Net earned premiums                             | \$183                                                               | \$142 |
| Net investment income                           | 99                                                                  | 101   |
| Net realized investment gains (losses)          | (13 )                                                               | 16    |
| Net change in fair value of credit derivatives: |                                                                     |       |
| Realized gains (losses) and other settlements   | 8                                                                   | 21    |
| Net unrealized gains (losses)                   | (68 )                                                               | 103   |
| Net change in fair value of credit derivatives  | (60 )                                                               | 124   |
| Fair value gains (losses) on CCS                | (16 )                                                               | 2     |
| Fair value gains (losses) on FG VIEs            | 18                                                                  | (7 )  |
| Other income (loss)                             | 34                                                                  | (9 )  |
| Total revenues                                  | 245                                                                 | 369   |
| Expenses:                                       |                                                                     |       |
| Loss and LAE                                    | 90                                                                  | 18    |
| Amortization of deferred acquisition costs      | 4                                                                   | 4     |
| Interest expense                                | 26                                                                  | 25    |
| Other operating expenses                        | 60                                                                  | 56    |
| Total expenses                                  | 180                                                                 | 103   |
| Income (loss) before provision for income taxes | 65                                                                  | 266   |
| Provision (benefit) for income taxes            | 6                                                                   | 65    |
| Net income (loss)                               | \$59                                                                | \$201 |

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## Net Earned Premiums

Net earned premiums are recognized over the contractual lives, or in the case of homogeneous pools of insured obligations, the remaining expected lives, of financial guaranty insurance contracts. The Company estimates remaining expected lives of its insured obligations and makes prospective adjustments for such changes in expected lives. Scheduled net earned premiums are expected to decrease each year unless replaced by a higher amount of new business, reassumptions of previously ceded business or books of business acquired in a business combination. See "Financial Guaranty Insurance Premiums" in Note 6, Financial Guaranty Insurance, of the Financial Statements, for additional information and the expected timing of future premium earnings.

## Net Earned Premiums

|                                             | First<br>Quarter<br>2016 2015<br>(in<br>millions) |       |
|---------------------------------------------|---------------------------------------------------|-------|
| Financial guaranty:                         |                                                   |       |
| Public finance                              |                                                   |       |
| Scheduled net earned premiums and accretion | \$69                                              | \$66  |
| Accelerations(1)                            | 79                                                | 40    |
| Total public finance                        | 148                                               | 106   |
| Structured finance(2)                       |                                                   |       |
| Scheduled net earned premiums and accretion | 25                                                | 34    |
| Accelerations(1)                            | 10                                                | 1     |
| Total structured finance                    | 35                                                | 35    |
| Other                                       | 0                                                 | 1     |
| Total net earned premiums                   | \$183                                             | \$142 |

(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 \$5 million and \$5 million for First Quarter 2016 and 2015, respectively related to consolidated FG VIEs.

Net earned premiums increased in First Quarter 2016 compared with First Quarter 2015 due primarily to higher accelerations and to net earned premiums related to the acquisition of Radian Asset, offset by the scheduled decline in structured finance par outstanding, as shown in the table above.

At March 31, 2016, \$3.6 billion of net deferred premium revenue remained to be earned over the life of the insurance contracts.

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## Net Investment Income

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets.

## Net Investment Income (1)

|                                                                | First<br>Quarter<br>2016 | 2015  |
|----------------------------------------------------------------|--------------------------|-------|
|                                                                | (in millions)            |       |
| Income from fixed-maturity securities managed by third parties | \$79                     | \$82  |
| Income from internally managed securities:                     |                          |       |
| Fixed maturities                                               | 17                       | 15    |
| Other                                                          | 5                        | 6     |
| Gross investment income                                        | 101                      | 103   |
| Investment expenses                                            | (2 )                     | (2 )  |
| Net investment income                                          | \$99                     | \$101 |

(1) Net investment income excludes \$5 million and \$3 million for First Quarter 2016 and 2015, respectively, related to consolidated FG VIEs.

Net investment income decreased due to lower average investment balances and lower book yield. The overall pre-tax book yield was 3.65% as of March 31, 2016 and 3.76% as of March 31, 2015, respectively. Excluding the internally managed portfolio, pre-tax book yield was 3.45% as of March 31, 2016 compared with 3.55% as of March 31, 2015.

## Net Realized Investment Gains (Losses)

The table below presents the components of net realized investment gains (losses). See Note 10, Investments and Cash, of the Financial Statements.

## Net Realized Investment Gains (Losses)

|                                                   | First<br>Quarter<br>2016 | 2015 |
|---------------------------------------------------|--------------------------|------|
|                                                   | (in<br>millions)         |      |
| Gross realized gains on the investment portfolio  | \$6                      | \$25 |
| Gross realized losses on the investment portfolio | (3 )                     | (2 ) |
| Other-than-temporary impairment                   | (16 )                    | (7 ) |
| Net realized investment gains (losses)            | \$(13)                   | \$16 |

Other-than-temporary-impairments in First Quarter 2016 and First Quarter 2015 were primarily attributable to securities purchased for loss mitigation purposes. Realized gains on the investment portfolio in First Quarter 2015 were due primarily to sales of securities in order to fund the purchase of Radian Asset by AGC.

## Other Income (Loss)

Other income (loss) is comprised of recurring items such as foreign exchange remeasurement gains and losses, ancillary fees on financial guaranty policies such as commitment, consent and processing fees, and if applicable, other revenue items on financial guaranty insurance and reinsurance contracts such as commutation gains on re-assumptions of previously ceded business, loss mitigation recoveries and certain non-recurring items.



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## Other Income (Loss)

|                                                                                       | First<br>Quarter<br>2016 | 2015   |
|---------------------------------------------------------------------------------------|--------------------------|--------|
|                                                                                       | (in<br>millions)         |        |
| Foreign exchange gain (loss) on remeasurement of premium receivable and loss reserves | \$(2 )                   | \$(13) |
| Other (1)                                                                             | 36                       | 4      |
| Total other income (loss)                                                             | \$34                     | \$(9 ) |

(1) Other in First Quarter 2016 represents primarily a benefit due to loss mitigation recoveries.

## Economic Loss Development

The insured portfolio includes policies accounted for under three separate accounting models depending on the characteristics of the contract and the Company's control rights. Please refer to Note 5, Expected Loss to be Paid, of the Financial Statements, for a discussion of the assumptions and methodologies used in calculating the expected loss to be paid for all contracts. For a discussion of the loss estimation process, approach to projecting losses in the U.S. RMBS portfolio and the measurement and recognition accounting policies under GAAP for each type of contract, see the following in Item 8, Financial Statements and Supplementary Data of the Company's Annual Report on Form 10-K:

- Note 5 for expected loss to be paid,
- Note 6 for financial guaranty insurance,
- Note 7 for fair value methodologies for credit derivatives and FG VIE assets and liabilities,
- Note 8 for credit derivatives, and
- Note 9 for consolidated FG VIEs.

The discussion of losses that follows encompasses losses on all contracts in the insured portfolio regardless of accounting model, unless otherwise specified. In order to effectively evaluate and manage the economics of the entire insured portfolio, management compiles and analyzes expected loss information for all policies on a consistent basis. That is, management monitors and assigns ratings and calculates expected losses in the same manner for all its exposures. Management also considers contract specific characteristics that affect the estimates of expected loss.

The surveillance process for identifying transactions with expected losses is described in the notes to the consolidated financial statements. More extensive monitoring and intervention is employed for all BIG surveillance categories, with internal credit ratings reviewed quarterly.

Net expected loss to be paid consists primarily of the present value of future: expected claim and loss adjustment expenses ("LAE") payments, expected recoveries from excess spread and other collateral in the transaction structures, cessions to reinsurers, and expected recoveries for breaches of R&W and the effects of other loss mitigation strategies. Current risk free rates are used to discount expected losses at the end of each reporting period and therefore changes in such rates from period to period affect the expected loss estimates reported. Assumptions used in the determination of the net expected loss to be paid such as delinquency, severity, and discount rates and expected timeframes to recovery in the mortgage market were consistent by sector regardless of the accounting model used. The primary drivers of economic loss development are discussed below. Changes in risk free rates used to discount losses affect economic loss development, loss and LAE, and non-GAAP loss expense; however the effect of changes in discount rates are not indicative of actual credit impairment or improvement in the period.

The primary differences between net economic loss development and loss and LAE reported under GAAP are that GAAP:

- considers deferred premium revenue in the calculation of loss reserves and loss expense for financial guaranty insurance contracts,

- eliminates losses related to FG VIEs and

- does not include estimated losses on credit derivatives.

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Loss expense reported in operating income (i.e. non-GAAP loss expense) includes losses on financial guaranty insurance, credit derivatives and FG VIEs.

For financial guaranty insurance contracts, a GAAP loss is generally recorded only when expected losses exceed deferred premium revenue. Therefore, the timing of loss recognition in income does not necessarily coincide with the timing of the actual credit impairment or improvement reported in net economic loss development. Transactions acquired in a business combination generally have the largest deferred premium revenue balances because of the purchase accounting adjustments made at acquisition. Therefore the largest differences between net economic loss development and loss expense relate to these policies. See "—Loss and LAE (Financial Guaranty Insurance Contracts)" below.

## Net Expected Loss to be Paid

|                                                             | As of<br>March<br>31,<br>2016<br>(in millions) | As of<br>December<br>31, 2015 |
|-------------------------------------------------------------|------------------------------------------------|-------------------------------|
| Public finance                                              | \$903                                          | \$ 809                        |
| Structured finance                                          |                                                |                               |
| U.S. RMBS before benefit for recoveries for breaches of R&W | 340                                            | 488                           |
| Net benefit for recoveries for breaches of R&W (1)          | (47 )                                          | (79 )                         |
| U.S. RMBS after benefit for recoveries for breaches of R&W  | 293                                            | 409                           |
| Other structured finance                                    | 141                                            | 173                           |
| Structured finance                                          | 434                                            | 582                           |
| Total                                                       | \$1,337                                        | \$ 1,391                      |

As of March 31, 2016 and December 31, 2015, the remaining estimated benefit for recoveries for breaches of (1)R&W are subject to contractual settlement agreements. The Company is no longer actively pursuing any R&W providers for breaches.

## Economic Loss Development (Benefit) (1)

|                                                             | First<br>Quarter<br>2016 | 2015<br>(in<br>millions) |
|-------------------------------------------------------------|--------------------------|--------------------------|
| Public finance                                              | \$99                     | \$ 6                     |
| Structured finance                                          |                          |                          |
| U.S. RMBS before benefit for recoveries for breaches of R&W | (50 )                    | (47 )                    |
| Net benefit for recoveries for breaches of R&W              | 19                       | 51                       |
| U.S. RMBS after benefit for recoveries for breaches of R&W  | (31 )                    | 4                        |
| Other structured finance                                    | (9 )                     | (13 )                    |
| Structured finance                                          | (40 )                    | (9 )                     |
| Total                                                       | \$59                     | \$(3 )                   |

(1) Economic loss development includes the effects of changes in assumptions based on observed market trends, changes in discount rates, accretion of discount and the economic effects of loss mitigation efforts.

#### First Quarter 2016 Net Economic Loss Development

Total economic loss development of \$59 million in First Quarter 2016 was generated mainly by the U.S. public finance sector, partially offset by a net benefit in the structured finance sector. The risk-free rates used to discount expected losses ranged from 0.0% to 2.88% as of March 31, 2016 and 0.0% to 3.25% as of December 31, 2015. The effect of the change in the risk-free rates used to discount expected losses was a loss of \$63 million in First Quarter 2016.

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U.S. Public Finance Economic Loss Development: The net par outstanding for U.S. public finance obligations rated BIG by the Company was \$8.0 billion as of March 31, 2016 compared with \$7.8 billion as of December 31, 2015. The Company projects that its total net expected loss across its troubled U.S. public finance credits as of March 31, 2016 will be \$864 million, compared with \$771 million as of December 31, 2015. Economic loss development in First Quarter 2016 was \$98 million, which was primarily attributable to Puerto Rico exposures. See "Insured Portfolio-Exposure to Puerto Rico" below for details about significant developments that have taken place in Puerto Rico.

U.S. RMBS Economic Loss Development: The net benefit attributable to U.S. RMBS was \$31 million due mainly to the acceleration of claim payments as a means of mitigating future losses on certain Alt-A transactions.

Other Structured Finance Economic Loss Development: The net benefit attributable to structured finance (excluding U.S. RMBS) was \$9 million, due primarily to the commutation of certain assumed student loan exposures.

First Quarter 2015 Net Economic Loss Development

Total economic loss development was a favorable \$3 million in First Quarter 2015, due primarily to performance improvements in trust preferred securities ("TruPS") and student loans, offset by modest increases in loss estimates on certain Puerto Rico exposures. The risk-free rates used to discount expected losses ranged from 0.0% to 2.89% as of March 31, 2015 and 0.0% to 2.95% as of December 31, 2014. Please refer to Note 5, Expected Loss to be Paid, of the Financial Statements, for additional information.

U.S. Public Finance Economic Loss Development: The net par outstanding for U.S. public finance obligations rated BIG by the Company was \$7.9 billion as of March 31, 2015 compared with \$7.9 billion as of December 31, 2014. The Company projected that its total net expected loss across its troubled U.S. public finance credits as of March 31, 2015 would be \$310 million, compared with \$303 million as of December 31, 2014. Economic loss development in First Quarter 2015 was approximately \$9 million, which was primarily attributable to certain Puerto Rico exposures.

U.S. RMBS Economic Loss Development: The net economic development attributable to U.S. RMBS of \$4 million was primarily due to modest underlying collateral deterioration. Certain of the Company's insured U.S. RMBS transactions benefited from a third-party settlement, which transactions are also covered by one of the Company's existing R&W settlement agreements. The resulting improvement in projected cash flows of the underlying transactions reduced the expected R&W benefit under the Company's settlement agreement. The net benefit of these agreements, after R&W, was \$7 million in First Quarter 2015.

Loss and LAE (Financial Guaranty Insurance Contracts)

For transactions accounted for as financial guaranty insurance under GAAP, each transaction's expected loss to be expensed, net of estimated recoveries, is compared with the deferred premium revenue of that transaction. Generally, when the expected loss to be expensed exceeds the deferred premium revenue, a loss is recognized in the income statement for the amount of such excess. When the Company measures operating income, a non-GAAP financial measure, it calculates the credit derivative and FG VIE losses incurred in a similar manner.

While expected loss to be paid is an important liquidity measure that provides the present value of amounts that the Company expects to pay or recover in future periods on all contracts, expected loss to be expensed is important because it presents the Company's projection of incurred losses that will be recognized in future periods as deferred premium revenue amortizes into income on financial guaranty insurance policies. Expected loss to be paid for FG VIEs pursuant to AGC's and AGM's financial guaranty policies is calculated in a manner consistent with financial guaranty insurance contracts, but eliminated in consolidation under GAAP.



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The following table presents the loss and LAE recorded in the consolidated statements of operations. These amounts are based on economic loss development and expected losses to be paid for financial guaranty insurance contracts only, and the amortization of the related unearned premium reserve on a transaction by transaction basis. Amounts presented are net of reinsurance.

Loss and LAE Reported  
on the Consolidated Statements of Operations

|                                                       | First<br>Quarter<br>2016 | 2015 |
|-------------------------------------------------------|--------------------------|------|
|                                                       | (in<br>millions)         |      |
| Public finance                                        | \$97                     | \$18 |
| Structured finance:                                   |                          |      |
| U.S. RMBS                                             | 11                       | 7    |
| Other structured finance                              | (11 )                    | (2 ) |
| Structured finance                                    | 0                        | 5    |
| Total insurance contracts before FG VIE consolidation | 97                       | 23   |
| Effect of consolidating FG VIEs                       | (7 )                     | (5 ) |
| Total loss and LAE (1)                                | \$90                     | \$18 |

(1) Excludes credit derivative benefit of \$6 million for First Quarter 2016 and credit derivative benefit of \$12 million for First Quarter 2015, which are included in non-GAAP loss expense.

Loss and LAE in First Quarter 2016 was mainly driven by higher loss reserves on certain Puerto Rico exposures partially offset by a benefit from the commutations of certain assumed student loan exposures.

In First Quarter 2015, losses incurred were due primarily to increased loss estimates on certain Puerto Rico exposures, partially offset by a benefit in student loans and insured TruPS transactions.

For financial guaranty contracts accounted for as insurance, the amounts reported in the GAAP financial statements may only reflect a portion of the current period's economic loss development and may also include a portion of prior-period economic loss development. The difference between economic loss development on financial guaranty insurance contracts and loss and LAE recognized in GAAP income relates to the effect of taking deferred premium revenue into account for GAAP loss and LAE, which is not considered in economic loss development.

The table below presents the expected timing of loss recognition for insurance contracts on both a reported GAAP net income and non-GAAP operating income basis.

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Financial Guaranty Insurance  
Net Expected Loss to be Expensed  
As of March 31, 2016

|                                    | In GAAP<br>Reported<br>Income<br>(in millions) | Non-GAAP<br>Operating<br>Income (1) |
|------------------------------------|------------------------------------------------|-------------------------------------|
| 2016 (April 1 – June 30)           | \$ 11                                          | \$ 14                               |
| 2016 (July 1 – September 30)       | 10                                             | 12                                  |
| 2016 (October 1 – December 31)     | 9                                              | 12                                  |
| 2017                               | 34                                             | 42                                  |
| 2018                               | 33                                             | 41                                  |
| 2019                               | 30                                             | 36                                  |
| 2020                               | 27                                             | 33                                  |
| 2021-2025                          | 100                                            | 117                                 |
| 2026-2030                          | 70                                             | 78                                  |
| 2031-2035                          | 45                                             | 54                                  |
| After 2035                         | 20                                             | 24                                  |
| Net expected loss to be expensed   | 389                                            | 463                                 |
| Future accretion                   | 156                                            | 189                                 |
| Total expected future loss and LAE | \$545                                          | \$ 652                              |

(1) Net expected loss to be expensed for GAAP reported income is different than operating income, a non-GAAP financial measure, by the amount related to consolidated FG VIEs and credit derivatives.

#### Net Change in Fair Value of Credit Derivatives

Changes in the fair value of credit derivatives occur primarily because of changes in interest rates, credit spreads, notional amounts, credit ratings of the referenced entities, expected terms, realized gains (losses) and other settlements, and the issuing company's own credit rating and credit spreads, and other market factors. With considerable volatility continuing in the market, unrealized gains (losses) on credit derivatives may fluctuate significantly in future periods.

Except for net estimated credit impairments (i.e., net expected payments), the unrealized gains and losses on credit derivatives are expected to reduce to zero as the exposure approaches its maturity date. Changes in the fair value of the Company's credit derivatives that do not reflect actual or expected claims or credit losses have no impact on the Company's statutory claims-paying resources, rating agency capital or regulatory capital positions. Expected losses to be paid in respect of contracts accounted for as credit derivatives are included in the discussion above "—Economic Loss Development."

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



from widening general market credit spreads, while a narrowing of the CDS prices traded on AGC and AGM has an effect of offsetting unrealized gains that result from narrowing general market credit spreads.

The valuation of the Company's credit derivative contracts requires the use of models that contain significant, unobservable inputs, and are classified as Level 3 in the fair value hierarchy. The models used to determine fair value are primarily developed internally based on market conventions for similar transactions that the Company observed in the past. There has been very limited new issuance activity in this market over the past several years and as of March 31, 2016, market prices for the Company's credit derivative contracts were generally not available. Inputs to the estimate of fair value include

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various market indices, credit spreads, the Company's own credit spread, and estimated contractual payments. See Note 7, Fair Value Measurement, of the Financial Statements for additional information.

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

|                                                                                                 | First Quarter |       |
|-------------------------------------------------------------------------------------------------|---------------|-------|
|                                                                                                 | 2016          | 2015  |
|                                                                                                 | (in millions) |       |
| Realized gains on credit derivatives                                                            | \$10          | \$23  |
| Net credit derivative losses (paid and payable) recovered and recoverable and other settlements | (2 )          | (2 )  |
| Realized gains (losses) and other settlements on credit derivatives (1)                         | 8             | 21    |
| Net change in unrealized gains (losses) on credit derivatives:                                  |               |       |
| Pooled corporate obligations                                                                    | (48 )         | 17    |
| U.S. RMBS                                                                                       | (15 )         | 75    |
| CMBS                                                                                            | 0             | 0     |
| Other                                                                                           | (5 )          | 11    |
| Net change in unrealized gains (losses) on credit derivatives                                   | (68 )         | 103   |
| Net change in fair value of credit derivatives                                                  | \$(60)        | \$124 |

(1) Includes realized gains and losses due to terminations and settlements of CDS contracts.

## Net Par and Realized Gains

## from Terminations and Settlements of Credit Derivative Contracts

|                                                   | First<br>Quarter<br>2016 | 2015  |
|---------------------------------------------------|--------------------------|-------|
|                                                   | (in<br>millions)         |       |
| Net par of terminated credit derivative contracts | \$ —                     | \$ 93 |
| Realized gains on credit derivatives              | 0                        | 11    |

During First Quarter 2016, unrealized fair value losses were generated primarily in the trust preferred, and U.S. RMBS prime first lien and subprime sectors, due to wider implied net spreads. The wider implied net spreads were primarily a result of the decreased cost to buy protection on AGC and AGM, particularly for the one year and five year CDS spread. These transactions were pricing at or above their floor levels (or the minimum rate at which the Company would consider assuming these risks based on historical experience); therefore when the cost of purchasing CDS protection on AGC and AGM, which management refers to as the CDS spread on AGC and AGM, decreased the implied spreads that the Company would expect to receive on these transactions increased. Unrealized fair value losses in the Other Sector were generated primarily by a price decline on a hedge the Company has against another financial guarantor. These losses were partially offset by an unrealized fair value gain on a terminated toll road securitization.

During First Quarter 2015, unrealized fair value gains were generated primarily in the U.S. RMBS prime first lien and adjustable rate mortgage ("Option ARM") sectors. The change in fair value of credit derivatives in First Quarter 2015 was primarily due to a refinement in methodology to address an instance in a U.S. RMBS transaction that changed from an expected loss to an expected recovery position. This refinement resulted in approximately \$49 million in fair value gains in First Quarter 2015. In addition, there were unrealized gains in the TruPS CDO and Other sectors as

result of price improvements on the underlying collateral. The changes in the Company's CDS spreads did not have a material impact during the quarter.

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## CDS Spread on AGC and AGM

Quoted price of CDS contract (in basis points)

|                       | As of<br>March<br>31,<br>2016 | As of<br>December<br>31, 2015 | As of<br>March<br>31,<br>2015 | As of<br>December<br>31, 2014 |
|-----------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|
| Five-year CDS spread: |                               |                               |                               |                               |
| AGC                   | 307                           | 376                           | 317                           | 323                           |
| AGM                   | 309                           | 366                           | 341                           | 325                           |
| One-year CDS spread   |                               |                               |                               |                               |
| AGC                   | 105                           | 139                           | 60                            | 80                            |
| AGM                   | 102                           | 131                           | 80                            | 85                            |

Effect of Changes in the Company's Credit Spread on  
Unrealized Gains (Losses) on Credit Derivatives

First Quarter  
2016 2015  
(in millions)

## Change in unrealized gains (losses) of credit derivatives:

|                                                                |        |       |
|----------------------------------------------------------------|--------|-------|
| Before considering implication of the Company's credit spreads | \$(27) | \$111 |
| Resulting from change in the Company's credit spreads          | (41 )  | (8 )  |
| After considering implication of the Company's credit spreads  | \$(68) | \$103 |

Management believes that the trading level of AGC's and AGM's credit spreads is due to the correlation between AGC's and AGM's risk profile, the current risk profile of the broader financial markets, and to increased demand for credit protection against AGC and AGM as the result of its financial guaranty volume, as well as the overall lack of liquidity in the CDS market. Offsetting the benefit attributable to AGC's and AGM's credit spread were higher credit spreads in the fixed income security markets relative to pre-financial crisis levels. The higher credit spreads in the fixed income security market are due to the lack of liquidity in the high-yield collateralized debt obligations ("CDO"), TruPS CDOs, and collateralized loan obligation ("CLO") markets as well as continuing market concerns over the 2005-2007 vintages of RMBS.

## Financial Guaranty Variable Interest Entities

As of March 31, 2016 and December 31, 2015, the Company consolidated 33 and 34 VIEs, respectively. The table below presents the effects on reported GAAP income resulting from consolidating these FG VIEs and eliminating their related insurance and investment accounts and, in total, represents a difference between GAAP reported net income and non-GAAP operating income attributable to FG VIEs. The consolidation of FG VIEs has a significant effect on net income and shareholders' equity due to:

- changes in fair value gains (losses) on FG VIE assets and liabilities,
- the eliminations of premiums and losses related to the AGC and AGM FG VIE liabilities with recourse, and
- the elimination of investment balances related to the Company's purchase of AGC and AGM insured FG VIE debt.

Upon consolidation of a FG VIE, the related insurance and, if applicable, the related investment balances, are considered intercompany transactions and therefore eliminated. See “—Non-GAAP Financial Measures—Operating Income” below and Note 9, Consolidated Variable Interest Entities, of the Financial Statements for more details.

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## Effect of Consolidating FG VIEs on Net Income

|                                        | First<br>Quarter<br>2016 2015<br>(in millions) |         |
|----------------------------------------|------------------------------------------------|---------|
| Net earned premiums                    | \$ (5 )                                        | \$ (5 ) |
| Net investment income                  | (5 )                                           | (3 )    |
| Net realized investment gains (losses) | 1                                              | 0       |
| Fair value gains (losses) on FG VIEs   | 18                                             | (7 )    |
| Loss and LAE                           | 6                                              | 5       |
| Effect on income before tax            | 15                                             | (10 )   |
| Less: tax provision (benefit)          | 5                                              | (4 )    |
| Effect on net income (loss)            | \$ 10                                          | \$ (6 ) |

Fair value gains (losses) on FG VIEs represent the net change in fair value on the consolidated FG VIEs' assets and liabilities. During First Quarter 2016, the Company recorded a pre-tax net fair value gain on consolidated FG VIEs of \$18 million. The primary driver of the gain was price appreciation on the FG VIE assets during the quarter resulting from improvements in the underlying collateral.

During First Quarter 2015, the Company recorded a pre-tax net fair value loss on consolidated FG VIEs of \$7 million. The primary driver of the loss was a pre-tax net fair value loss of \$26 million on the consolidation of one new FG VIE. The net fair value loss on consolidation was partially offset by net gains due to price appreciation on the FG VIE assets during the quarter resulting from improvements in the underlying collateral.

## Provision for Income Tax

## Provision for Income Taxes and Effective Tax Rates

|                                            | First<br>Quarter<br>2016 2015<br>(in millions) |       |
|--------------------------------------------|------------------------------------------------|-------|
| Total provision (benefit) for income taxes | \$6                                            | \$65  |
| Effective tax rate                         | 10.0%                                          | 24.2% |

The Company's effective tax rates reflect the proportion of income recognized by each of the Company's operating subsidiaries, with U.S. subsidiaries taxed at the U.S. marginal corporate income tax rate of 35%, U.K. subsidiaries taxed at the U.K. marginal corporate tax rate of 20% unless subject to U.S. tax by election or as a U.S. controlled foreign corporation, and no taxes for the Company's Bermuda subsidiaries unless subject to U.S. tax by election or as a U.S. controlled foreign corporation. The Company's overall corporate effective tax rate fluctuates based on the distribution of taxable income across these jurisdictions. In each of the periods presented, the portion of taxable income from each jurisdiction varied. The non-taxable book to tax differences were consistent as compared to the prior period. The effective tax rate is lower in 2016, due to a higher ratio of tax exempt investment income to pre-tax income.

## Non-GAAP Financial Measures

To reflect the key financial measures management analyzes in evaluating the Company's operations and progress towards long-term goals, the Company discusses both measures determined in accordance with GAAP and measures not promulgated in accordance with GAAP ("non-GAAP financial measures"). Although the financial measures identified as non-GAAP should not be considered substitutes for GAAP measures, management considers them key performance indicators and employs them as well as other factors in determining compensation. Non-GAAP financial measures, therefore, provide investors with important information about the key financial measures management utilizes in measuring its business. The primary limitation of non-GAAP financial measures is the potential lack of comparability to those of other companies, which may define non-GAAP measures differently because there is limited literature with respect to such measures. Three of the primary non-GAAP financial measures analyzed by the Company's senior management are: operating income, adjusted book value and PVP.

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Management and the board of directors utilize non-GAAP financial measures in evaluating the Company's financial performance. By providing these non-GAAP financial measures, the Company gives investors, analysts and financial news reporters access to the same information that management reviews internally. In addition, Assured Guaranty's presentation of non-GAAP financial measures is consistent with how analysts calculate their estimates of Assured Guaranty's financial results in their research reports on Assured Guaranty and with how investors, analysts and the financial news media evaluate Assured Guaranty's financial results.

The following paragraphs define each non-GAAP financial measure and describe why it is useful. A reconciliation of the non-GAAP financial measure and the most directly comparable GAAP financial measure, is also presented below.

### Operating Income

Management believes that operating income is a useful measure because it clarifies the understanding of the underwriting results of the Company's financial guaranty business, and also includes financing costs and net investment income, and enables investors and analysts to evaluate the Company's financial results as compared with the consensus analyst estimates distributed publicly by financial databases. Operating income is defined as net income (loss) attributable to AGL, as reported under GAAP, adjusted for the following:

1) Elimination of the after-tax realized gains (losses) on the Company's investments, except for gains and losses on securities classified as trading. The timing of realized gains and losses, which depends largely on market credit cycles, can vary considerably across periods. The timing of sales is largely subject to the Company's discretion and influenced by market opportunities, as well as the Company's tax and capital profile. Trends in the underlying profitability of the Company's business can be more clearly identified without the fluctuating effects of these transactions.

2) Elimination of the after-tax non-credit-impairment unrealized fair value gains (losses) on credit derivatives, which is the amount in excess of the present value of the expected estimated economic credit losses, and non-economic payments. Such fair value adjustments are heavily affected by, and in part fluctuate with, changes in market interest rates, credit spreads and other market factors and are not expected to result in an economic gain or loss. Additionally, such adjustments present all financial guaranty contracts on a more consistent basis of accounting, whether or not they are subject to derivative accounting rules.

3) Elimination of the after-tax fair value gains (losses) on the Company's CCS. Such amounts are heavily affected by, and in part fluctuate with, changes in market interest rates, credit spreads and other market factors and are not expected to result in an economic gain or loss.

4) Elimination of the after-tax foreign exchange gains (losses) on remeasurement of net premium receivables and loss and LAE reserves. Long-dated receivables constitute a significant portion of the net premium receivable balance and represent the present value of future contractual or expected collections. Therefore, the current period's foreign exchange remeasurement gains (losses) are not necessarily indicative of the total foreign exchange gains (losses) that the Company will ultimately recognize.

5) Elimination of the effects of consolidating FG VIEs in order to present all financial guaranty contracts on a more consistent basis of accounting, whether or not GAAP requires consolidation. GAAP requires the Company to consolidate certain VIEs that have issued debt obligations insured by the Company even though the Company does not own such VIEs.





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to Operating Income

|                                                                                                   | First Quarter |        |
|---------------------------------------------------------------------------------------------------|---------------|--------|
|                                                                                                   | 2016          | 2015   |
|                                                                                                   | (in millions) |        |
| Net income (loss)                                                                                 | \$59          | \$201  |
| Less after-tax adjustments:                                                                       |               |        |
| Realized gains (losses) on investments                                                            | (9 )          | 9      |
| Non-credit impairment unrealized fair value gains (losses) on credit derivatives                  | (43 )         | 66     |
| Fair value gains (losses) on CCS                                                                  | (10 )         | 1      |
| Foreign exchange gains (losses) on remeasurement of premiums receivable and loss and LAE reserves | (2 )          | (9 )   |
| Effect of consolidating FG VIEs                                                                   | 10            | (6 )   |
| Operating income                                                                                  | \$113         | \$140  |
| Effective tax rate on operating income                                                            | 20.3 %        | 22.1 % |

## Adjusted Book Value and Operating Shareholders' Equity

Management also uses adjusted book value to measure the intrinsic value of the Company, excluding franchise value. Growth in adjusted book value per share is one of the key financial measures used in determining the amount of certain long term compensation to management and employees and used by rating agencies and investors.

Management believes that operating shareholders' equity is a useful measure because it presents the equity of the Company with all financial guaranty contracts accounted for on a more consistent basis and excludes fair value adjustments that are not expected to result in economic gain or loss. Many investors, analysts and financial news reporters use operating shareholders' equity as the principal financial measure for valuing AGL's current share price or projected share price and also as the basis of their decision to recommend, buy or sell AGL's common shares. Many of the Company's fixed income investors also use operating shareholders' equity to evaluate the Company's capital adequacy. Operating shareholders' equity is the basis of the calculation of adjusted book value (see below). Operating shareholders' equity is defined as shareholders' equity attributable to AGL, as reported under GAAP, adjusted for the following:

- 1) Elimination of the effects of consolidating FG VIEs in order to present all financial guaranty contracts on a more consistent basis of accounting, whether or not GAAP requires consolidation. GAAP requires the Company to consolidate certain VIEs that have issued debt obligations insured by the Company even though the Company does not own such VIEs.
- 2) Elimination of the after-tax non-credit-impairment unrealized fair value gains (losses) on credit derivatives, which is the amount in excess of the present value of the expected estimated economic credit losses, and non-economic payments. Such fair value adjustments are heavily affected by, and in part fluctuate with, changes in market interest rates, credit spreads and other market factors and are not expected to result in an economic gain or loss.
- 3) Elimination of the after-tax fair value gains (losses) on the Company's CCS. Such amounts are heavily affected by, and in part fluctuate with, changes in market interest rates, credit spreads and other market factors and are not expected to result in an economic gain or loss.
- 4)

Elimination of the after-tax unrealized gains (losses) on the Company's investments that are recorded as a component of accumulated other comprehensive income ("AOCI") (excluding foreign exchange remeasurement). The AOCI component of the fair value adjustment on the investment portfolio is not deemed economic because the Company generally holds these investments to maturity and therefore should not recognize an economic gain or loss.

Management believes that adjusted book value is a useful measure because it enables an evaluation of the net present value of the Company's in-force premiums and revenues in addition to operating shareholders' equity. The premiums and

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revenues included in adjusted book value will be earned in future periods, but actual earnings may differ materially from the estimated amounts used in determining current adjusted book value due to changes in foreign exchange rates, prepayment speeds, terminations, credit defaults and other factors. Many investors, analysts and financial news reporters use adjusted book value to evaluate AGL's share price and as the basis of their decision to recommend, buy or sell the AGL common shares. Adjusted book value is operating shareholders' equity, as defined above, further adjusted for the following:

1) Elimination of after-tax deferred acquisition costs, net. These amounts represent net deferred expenses that have already been paid or accrued and will be expensed in future accounting periods.

2) Addition of the after-tax net present value of estimated net future credit derivative revenue. See below.

Addition of the after-tax value of the unearned premium reserve on financial guaranty contracts in excess of expected loss to be expensed, net of reinsurance. This amount represents the expected future net earned premiums, net of expected losses to be expensed, which are not reflected in GAAP equity.

#### Net Present Value of Estimated Net Future Credit Derivative Revenue

Management believes that this amount is a useful measure because it enables an evaluation of the value of future estimated credit derivative revenue. There is no corresponding GAAP financial measure. This amount represents the present value of estimated future revenue from the Company's credit derivative in-force book of business, net of reinsurance, ceding commissions and premium taxes, for contracts without expected economic losses, and is discounted at 6%. Estimated net future credit derivative revenue may change from period to period due to changes in foreign exchange rates, prepayment speeds, terminations, credit defaults or other factors that affect par outstanding or the ultimate maturity of an obligation.

#### Reconciliation of Shareholders' Equity to Adjusted Book Value

|                                                                                                              | As of March 31,<br>2016                            |           | As of December<br>31, 2015 |           |
|--------------------------------------------------------------------------------------------------------------|----------------------------------------------------|-----------|----------------------------|-----------|
|                                                                                                              | Total                                              | Per Share | Total                      | Per Share |
|                                                                                                              | (dollars in millions, except<br>per share amounts) |           |                            |           |
| Shareholders' equity                                                                                         | \$6,113                                            | \$ 45.26  | \$6,063                    | \$ 43.96  |
| Less after-tax adjustments:                                                                                  |                                                    |           |                            |           |
| Effect of consolidating FG VIEs                                                                              | (12 )                                              | (0.09 )   | (23 )                      | (0.16 )   |
| Non-credit impairment unrealized fair value gains (losses) on credit derivatives                             | (203 )                                             | (1.50 )   | (160 )                     | (1.16 )   |
| Fair value gains (losses) on CCS                                                                             | 30                                                 | 0.22      | 40                         | 0.29      |
| Unrealized gain (loss) on investment portfolio excluding foreign exchange effect                             | 344                                                | 2.55      | 260                        | 1.88      |
| Operating shareholders' equity                                                                               | 5,954                                              | 44.08     | 5,946                      | 43.11     |
| After-tax adjustments:                                                                                       |                                                    |           |                            |           |
| Less: Deferred acquisition costs                                                                             | 145                                                | 1.07      | 147                        | 1.06      |
| Plus: Net present value of estimated net future credit derivative revenue                                    | 91                                                 | 0.67      | 116                        | 0.84      |
| Plus: Net unearned premium reserve on financial guaranty contracts in excess of expected loss to be expensed | 2,394                                              | 17.72     | 2,524                      | 18.29     |
| Adjusted book value                                                                                          | \$8,294                                            | \$ 61.40  | \$8,439                    | \$ 61.18  |

Shareholder's equity increased since December 31, 2015 due primarily to positive income and net unrealized gains on available for sale investment securities recorded in AOCI, which was partially offset by share repurchases and dividends. While operating shareholders' equity increased slightly, adjusted book value decreased since December 31, 2015 due mainly to share repurchases and dividends. Operating shareholders' equity per share and adjusted book value per share benefited from the repurchase of 3.0 million common shares through March 31, 2016.

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## PVP or Present Value of New Business Production

Management believes that PVP is a useful measure because it enables the evaluation of the value of new business production for the Company by taking into account the value of estimated future installment premiums on all new contracts underwritten in a reporting period as well as premium supplements and additional installment premium on existing contracts as to which the issuer has the right to call the insured obligation but has not exercised such right, whether in insurance or credit derivative contract form, which GAAP gross premiums written and the net credit derivative premiums received and receivable portion of net realized gains and other settlements on credit derivatives ("Credit Derivative Revenues") do not adequately measure. PVP in respect of financial guaranty contracts written in a specified period is defined as gross upfront and installment premiums received and the present value of gross estimated future installment premiums, in each case, discounted at 6%. For purposes of the PVP calculation, management discounts estimated future installment premiums on insurance contracts at 6%, while under GAAP, these amounts are discounted at a risk free rate. Additionally, under GAAP, management records future installment premiums on financial guaranty insurance contracts covering non-homogeneous pools of assets based on the contractual term of the transaction, whereas for PVP purposes, management records an estimate of the future installment premiums the Company expects to receive, which may be based upon a shorter period of time than the contractual term of the transaction. Actual future net earned or written premiums and Credit Derivative Revenues may differ from PVP due to factors including, but not limited to, changes in foreign exchange rates, prepayment speeds, terminations, credit defaults, or other factors that affect par outstanding or the ultimate maturity of an obligation.

## Reconciliation of PVP to Gross Written Premiums

|                                                                         | First<br>Quarter<br>2016 2015<br>(in<br>millions) |      |
|-------------------------------------------------------------------------|---------------------------------------------------|------|
| Total PVP                                                               | \$38                                              | \$36 |
| Less: PVP of non-financial guaranty insurance                           | 0                                                 | 6    |
| PVP of financial guaranty insurance                                     | 38                                                | 30   |
| Less: Financial guaranty installment premium PVP                        | 7                                                 | 17   |
| Total: Financial guaranty upfront gross written premiums                | 31                                                | 13   |
| Plus: Installment gross written premiums and other GAAP adjustments (1) | (12 )                                             | 19   |
| Total gross written premiums                                            | \$19                                              | \$32 |

Includes present value of new business on installment policies, gross written premium adjustments on existing (1) installment policies due to changes in assumptions, any cancellations of assumed reinsurance contracts, and other GAAP adjustments.

## Insured Portfolio

The following tables present the insured portfolio by asset class net of cessions to reinsurers. It includes all financial guaranty contracts outstanding as of the dates presented, regardless of the form written (i.e., credit derivative form or traditional financial guaranty insurance form) or the applicable accounting model (i.e., insurance, derivative or VIE consolidation). The Company excludes amounts attributable to loss mitigation securities (unless otherwise indicated) from par and principal and interest ("Debt Service") outstanding because it manages such securities as investments not insurance exposures.



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## Net Par Outstanding and Average Internal Rating by Sector

| Sector                                                  | As of March 31,<br>2016                         |                | As of December<br>31, 2015 |                |
|---------------------------------------------------------|-------------------------------------------------|----------------|----------------------------|----------------|
|                                                         | Net Par<br>Outstanding<br>(dollars in millions) | Avg.<br>Rating | Net Par<br>Outstanding     | Avg.<br>Rating |
| Public finance:                                         |                                                 |                |                            |                |
| U.S.:                                                   |                                                 |                |                            |                |
| General obligation                                      | \$121,800                                       | A              | \$126,255                  | A              |
| Tax backed                                              | 57,218                                          | A              | 58,062                     | A              |
| Municipal utilities                                     | 45,086                                          | A              | 45,936                     | A              |
| Transportation                                          | 22,531                                          | A              | 23,454                     | A              |
| Healthcare                                              | 14,631                                          | A              | 15,006                     | A              |
| Higher education                                        | 11,535                                          | A              | 11,936                     | A              |
| Infrastructure finance                                  | 3,145                                           | BBB            | 4,993                      | BBB            |
| Housing                                                 | 1,932                                           | A-             | 2,037                      | A              |
| Investor-owned utilities                                | 915                                             | A-             | 916                        | A-             |
| Other public finance—U.S.                               | 3,262                                           | A              | 3,271                      | A              |
| Total public finance—U.S.                               | 282,055                                         | A              | 291,866                    | A              |
| Non-U.S.:                                               |                                                 |                |                            |                |
| Infrastructure finance                                  | 12,673                                          | BBB            | 12,728                     | BBB            |
| Regulated utilities                                     | 9,907                                           | BBB+           | 10,048                     | BBB+           |
| Pooled infrastructure                                   | 1,831                                           | AA             | 1,879                      | AA             |
| Other public finance                                    | 4,974                                           | A              | 4,922                      | A              |
| Total public finance—non-U.S.                           | 29,385                                          | BBB+           | 29,577                     | BBB+           |
| Total public finance                                    | 311,440                                         | A              | 321,443                    | A              |
| Structured finance:                                     |                                                 |                |                            |                |
| U.S.:                                                   |                                                 |                |                            |                |
| Pooled corporate obligations                            | 15,380                                          | AAA            | 16,008                     | AAA            |
| RMBS                                                    | 6,677                                           | BBB-           | 7,067                      | BBB-           |
| Insurance securitizations                               | 2,900                                           | A+             | 3,000                      | A+             |
| Consumer receivables                                    | 2,084                                           | A-             | 2,099                      | A-             |
| Financial products                                      | 1,824                                           | AA-            | 1,906                      | AA-            |
| CMBS and other commercial real estate related exposures | 498                                             | AAA            | 533                        | AAA            |
| Commercial receivables                                  | 382                                             | BBB+           | 427                        | BBB+           |
| Other structured finance—U.S.                           | 707                                             | AA-            | 730                        | AA-            |
| Total structured finance—U.S.                           | 30,452                                          | AA-            | 31,770                     | AA-            |
| Non-U.S.:                                               |                                                 |                |                            |                |
| Pooled corporate obligations                            | 3,465                                           | AA             | 3,645                      | AA             |
| Commercial receivables                                  | 541                                             | BBB+           | 600                        | BBB+           |
| RMBS                                                    | 504                                             | BBB            | 492                        | BBB            |
| Other structured finance                                | 613                                             | AA-            | 621                        | AA-            |
| Total structured finance—non-U.S.                       | 5,123                                           | AA-            | 5,358                      | AA-            |
| Total structured finance                                | 35,575                                          | AA-            | 37,128                     | AA-            |
| Total net par outstanding                               | \$347,015                                       | A              | \$358,571                  | A              |





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The following tables set forth the Company's net financial guaranty portfolio by internal rating.

## Financial Guaranty Portfolio by Internal Rating

As of March 31, 2016

| Rating<br>Category               | Public Finance<br>U.S. |       |                  | Public Finance<br>Non-U.S. |       |                  | Structured Finance<br>U.S |       |                  | Structured Finance<br>Non-U.S |       |                  | Total     |       |                  |
|----------------------------------|------------------------|-------|------------------|----------------------------|-------|------------------|---------------------------|-------|------------------|-------------------------------|-------|------------------|-----------|-------|------------------|
|                                  | Net Par                |       | %<br>Outstanding | Net Par                    |       | %<br>Outstanding | Net Par                   |       | %<br>Outstanding | Net Par                       |       | %<br>Outstanding | Net Par   |       | %<br>Outstanding |
|                                  |                        |       |                  |                            |       |                  |                           |       |                  |                               |       |                  |           |       |                  |
|                                  | (dollars in millions)  |       |                  |                            |       |                  |                           |       |                  |                               |       |                  |           |       |                  |
| AAA                              | \$2,541                | 0.9   | %                | \$688                      | 2.3   | %                | \$13,953                  | 45.8  | %                | \$2,529                       | 49.4  | %                | \$19,711  | 5.7   | %                |
| AA                               | 65,310                 | 23.2  |                  | 1,969                      | 6.7   |                  | 7,505                     | 24.7  |                  | 154                           | 3.0   |                  | 74,938    | 21.6  |                  |
| A                                | 145,515                | 51.6  |                  | 6,695                      | 22.8  |                  | 2,584                     | 8.5   |                  | 551                           | 10.8  |                  | 155,345   | 44.7  |                  |
| BBB                              | 60,736                 | 21.5  |                  | 18,622                     | 63.4  |                  | 1,279                     | 4.2   |                  | 1,267                         | 24.7  |                  | 81,904    | 23.6  |                  |
| BIG                              | 7,953                  | 2.8   |                  | 1,411                      | 4.8   |                  | 5,131                     | 16.8  |                  | 622                           | 12.1  |                  | 15,117    | 4.4   |                  |
| Total net par<br>outstanding (1) | \$282,055              | 100.0 | %                | \$29,385                   | 100.0 | %                | \$30,452                  | 100.0 | %                | \$5,123                       | 100.0 | %                | \$347,015 | 100.0 | %                |

(1) Excludes \$1.5 billion of loss mitigation securities insured and held by the Company as of March 31, 2016, which are primarily BIG.

## Financial Guaranty Portfolio by Internal Rating

As of December 31, 2015

| Rating<br>Category               | Public Finance<br>U.S. |        |                  | Public Finance<br>Non-U.S. |        |                  | Structured Finance<br>U.S |        |                  | Structured Finance<br>Non-U.S |        |                  | Total     |        |                  |
|----------------------------------|------------------------|--------|------------------|----------------------------|--------|------------------|---------------------------|--------|------------------|-------------------------------|--------|------------------|-----------|--------|------------------|
|                                  | Net Par                |        | %<br>Outstanding | Net Par                    |        | %<br>Outstanding | Net Par                   |        | %<br>Outstanding | Net Par                       |        | %<br>Outstanding | Net Par   |        | %<br>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<br>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.

## Exposure to Puerto Rico

The Company has insured exposure to 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 March 31, 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.

In June 2014, the Puerto Rico legislature passed the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (the "Recovery Act") in order to provide a legislative framework for certain public corporations experiencing severe financial stress to restructure their debt, including Puerto Rico Highway and Transportation Authority ("PRHTA") and PREPA. Subsequently, the Commonwealth stated PREPA might need to seek relief under the Recovery Act due to liquidity constraints. Investors in bonds issued by PREPA filed suit in the United States District Court for the District of Puerto Rico challenging the Recovery Act. On February 6, 2015, the U.S. District Court for the District of Puerto Rico ruled the Recovery Act is preempted by the U.S. Bankruptcy Code and is therefore void. On July 6, 2015, the U.S. Court of Appeals for the First Circuit upheld that ruling, and on December 4, 2015, the U.S. Supreme Court granted petitions for writs of certiorari relating to that ruling. Oral

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arguments were held on March 22, 2016. Typical Supreme Court practice suggests a decision could be announced in June 2016, but there is no assurance that an opinion will be announced at such time, especially in light of the Supreme Court vacancy.

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, is unpayable and that a comprehensive debt restructuring may be necessary, and he has made similar statements since then.

On September 9, 2015, the Working Group for the Fiscal and Economic Recovery of Puerto Rico ("Working Group") established by the Governor published its "Puerto Rico Fiscal and Economic Growth Plan" (the "FEGP"). The FEGP included a recommendation that the Commonwealth's advisors begin to work on a voluntary exchange offer to its creditors as part of the FEGP.

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 PRHTA, Puerto Rico Infrastructure Finance 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 impacted by 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. For those PRIFA bonds the Company had insured, the Company paid approximately \$451 thousand of claims for the interest payments on which PRIFA had defaulted.

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 a moratorium, entity by entity, on debt service payments on debt of the commonwealth and its related authorities and public corporations, as well as instituting a stay against related litigation, among other things. It is possible that a court may find any attempt to exercise the power to declare a moratorium on debt service payments purportedly granted by the Moratorium Act to be unconstitutional, and the impact of any attempt to exercise such power on the Puerto Rico credits insured by the Company is uncertain. Shortly after signing it into law, the Governor used the authority of the Moratorium Act to declare an emergency period with respect to the Government Development Bank (the "GDB"), placing restrictions on its disbursements and certain of its other activities and moving the clearing of payroll of Commonwealth and GDB employees from the GDB.

On April 30, 2016, the Governor signed an order under the Moratorium Act ordering a moratorium on the debt service payment of approximately \$422 million due to be made by the GDB on May 2, 2016. On May 1, 2016, the GDB announced a tentative agreement with a group of creditors of the GDB (the "Ad Hoc Group") for a restructuring of GDB's notes and that the GDB would pay the interest due on May 2, 2016. According to the announcement, the Ad Hoc Group agreed to forbear from initiating litigation for 30 days during the pendency of negotiations. The GDB noted in its May 1 announcement that the tentative agreement requires 100% participation of the GDB's creditors and that it would be unlikely to reach that level of participation without a restructuring law enabling it to bind non-consenting creditors. The Company does not insure any debt issued by the GDB.

There have been a number of other proposals, plans and legislative initiatives offered in Puerto Rico and in the United States aimed at addressing Puerto Rico's fiscal issues. Among the responses proposed is a federal financial control board and access to bankruptcy courts or another restructuring mechanism. In addition, the Working Group has made several proposals for voluntary exchanges that include terms such as discounts, extensions and subordination. The final shape and timing of responses to Puerto Rico's distress eventually enacted or implemented by Puerto Rico or the

United States, if any, and the impact of any such actions on obligations insured by the Company, is uncertain and may differ substantially from the recommendations of the Working Group or any other proposals or plans described in the press or offered to date or in the future.

Standard & Poor's Ratings Services ("S&P"), Moody's Investors Service, Inc. ("Moody's") and Fitch Ratings have lowered the credit rating of the Commonwealth's bonds and on its public corporations several times over the past approximately two years, and the Commonwealth has disclosed its liquidity has been adversely affected by rating agency downgrades and by the limited market access for its debt, and also noted it has relied on short-term financings and interim loans from the GDB and other private lenders, which reliance has constrained its liquidity and increased its near-term refinancing risk.

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### PREPA

As of March 31, 2016, the Company had \$744 million insured net par outstanding of PREPA obligations. On July 1, 2015, PREPA made full payment of the \$416 million of principal and interest due on its bonds, including bonds insured by AGM and AGC. However, that payment was conditioned on and facilitated by AGM and AGC agreeing, also on July 1, to purchase a portion of \$131 million of interest-bearing bonds to help replenish certain of the operating funds PREPA used to make the \$416 million of principal and interest payments. On July 31, 2015, AGM and AGC purchased \$74 million aggregate principal amount of those bonds; the bonds were repaid in full in 2016.

On December 24, 2015, AGM and AGC entered into a 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, which enables PREPA to achieve debt relief and more efficient capital markets financing, Assured Guaranty will issue surety insurance policies in an aggregate amount not expected to exceed \$113 million in exchange for a market premium and 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. The Company's share of the bridge financing is approximately \$15 million. Legislation meeting the requirements of the RSA was enacted on February 16, 2016. The closing of the restructuring transaction, the issuance of the surety bonds and the closing of the bridge financing are subject to certain conditions, including confirmation that the enacted legislation meets all requirements of the RSA and execution of acceptable documentation and legal opinions.

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 restructuring of the insured PREPA revenue bonds, will be implemented. In addition, the impact of 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.

### PRHTA

As of March 31, 2016, the Company had \$910 million insured net par outstanding of PRHTA (Transportation revenue) bonds and \$369 million net par of PRHTA (Highway revenue) bonds. 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.

### Puerto Rico Sales Tax Financing Corporation ("COFINA")

As of March 31, 2016, the Company had \$270 million insured net par outstanding of junior COFINA bonds, which are secured by a lien on certain sales and use taxes. There have been proposals from both the Commonwealth and from holders of certain senior COFINA bonds to restructure COFINA debt.

### Puerto Rico Convention Center District Authority

As of March 31, 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.

### Puerto Rico Aqueduct and Sewer Authority ("PRASA")

As of March 31, 2016, the Company had \$388 million insured par outstanding to PRASA bonds, which are secured by the gross revenues of the system. On September 15, 2015, PRASA entered into a settlement with the U.S. Justice Department 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, it owed its contractors \$140 million.

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Municipal Finance Agency

As of March 31, 2016, the Company had \$387 million net par outstanding of bonds issued by the Puerto Rico Municipal Finance Agency (“MFA”) secured by a pledge of local property tax revenues. On October 13, 2015, the Company filed a motion to intervene in litigation between Centro de Recaudación de Ingresos Municipales (“CRIM”) and the GDB in which CRIM was seeking to ensure that the pledged tax revenues are, and will continue to be, available to support the MFA bonds. While the Company’s motion to intervene was denied, the GDB and CRIM have reported that they executed a new deed of trust that requires the GDB, as fiduciary, to keep the pledged tax revenues separate from any other GDB monies or accounts and that governs the manner in which the pledged revenues may be invested and dispersed.



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Net Exposure to Puerto Rico  
As of March 31, 2016

|                                                              | Net Par Outstanding |                  |                        |                  | Total Net           |                       |                 |
|--------------------------------------------------------------|---------------------|------------------|------------------------|------------------|---------------------|-----------------------|-----------------|
|                                                              | AGM Consolidated    | AGC Consolidated | AG Re (1) Consolidated | Eliminations (2) | Par Outstanding (4) | Gross Par Outstanding | Internal Rating |
| (in millions)                                                |                     |                  |                        |                  |                     |                       |                 |
| Exposures Previously Subject to the Voided Recovery Act(3):  |                     |                  |                        |                  |                     |                       |                 |
| PRHTA (Transportation revenue) (5)                           | \$289               | \$ 476           | \$ 225                 | \$ (80 )         | \$ 910              | \$ 937                | CCC-            |
| PREPA                                                        | 431                 | 74               | 239                    | —                | 744                 | 902                   | CC              |
| PRASA                                                        | —                   | 296              | 92                     | —                | 388                 | 388                   | CCC             |
| PRHTA (Highway revenue) (5)                                  | 219                 | 100              | 50                     | —                | 369                 | 574                   | CCC             |
| PRCCDA (5)                                                   | —                   | 82               | 82                     | —                | 164                 | 164                   | CCC-            |
| Total                                                        | 939                 | 1,028            | 688                    | (80 )            | 2,575               | 2,965                 |                 |
| Exposures Not Previously Subject to the Voided Recovery Act: |                     |                  |                        |                  |                     |                       |                 |
| Commonwealth of Puerto Rico - General Obligation Bonds       | 720                 | 415              | 480                    | —                | 1,615               | 1,738                 | CCC             |
| MFA                                                          | 206                 | 65               | 116                    | —                | 387                 | 570                   | CCC-            |
| COFINA                                                       | 262                 | —                | 8                      | —                | 270                 | 270                   | CCC+            |
| Puerto Rico Public Buildings Authority                       | 13                  | 137              | 38                     | —                | 188                 | 194                   | CCC             |
| PRIFA (5) (6)                                                | —                   | 10               | 8                      | —                | 18                  | 18                    | C               |
| University of Puerto Rico                                    | —                   | 1                | —                      | —                | 1                   | 1                     | CCC-            |
| Total                                                        | 1,201               | 628              | 650                    | —                | 2,479               | 2,791                 |                 |
| Total net exposure to Puerto Rico                            | \$2,140             | \$ 1,656         | \$ 1,338               | \$ (80 )         | \$ 5,054            | \$ 5,756              |                 |

(1) "AG Re" means Assured Guaranty Re Ltd.

(2) Net par outstanding eliminations relate to second-to-pay policies under which an Assured Guaranty insurance subsidiary guarantees an obligation already insured by another Assured Guaranty insurance subsidiary.

(3) On February 6, 2015, the U.S. District Court for the District of Puerto Rico ruled that the Recovery Act is preempted by the U.S. Bankruptcy Code and is therefore void. On July 6, 2015, the U.S. Court of Appeals for the First Circuit upheld that ruling, and on December 4, 2015, the U.S. Supreme Court granted petitions for writs of certiorari relating to that ruling.

(4) Includes exposure to capital appreciation bonds with a current aggregate net par outstanding of \$34 million and a fully accreted net par at maturity of \$67 million. Of these amounts, current net par of \$18 million and fully accreted net par at maturity of \$50 million relate to the Puerto Rico Sales Tax Financing Corporation, current net par of \$10 million and fully accreted net par at maturity of \$11 million relate to the PRHTA, and current net par of \$5 million and fully accreted net par at maturity of \$5 million relate to the Commonwealth General Obligation Bonds.

(5) The Governor issued executive orders on November 30, 2015 and December 8, 2015, directing the Puerto Rico Department of Treasury and the Puerto Rico Tourism Company to retain or transfer certain taxes and revenues pledged to secure the payment of bonds issued by PRHTA, PRIFA and 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 and revenues is unconstitutional, and demanding declaratory and injunctive relief.

(6)

On January 1, 2016 PRIFA defaulted on full payment of a portion of the interest due on its bonds on that date. For those PRIFA bonds the Company had insured, the Company paid approximately \$451 thousand of claims for the interest payments on which PRIFA had defaulted.

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The following table shows the scheduled amortization of the general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations insured by the Company. 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 pay the shortfall between the principal and interest due in any given period and the amount paid by the obligors.

## Amortization Schedule

of Net Par Outstanding of Puerto Rico

As of March 31, 2016

|                                                                                                                                                | Scheduled Net Par Amortization |              |      |      |      |      |      |      |      |      |      |               |               |               |               |               | Total |       |
|------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------|--------------|------|------|------|------|------|------|------|------|------|---------------|---------------|---------------|---------------|---------------|-------|-------|
|                                                                                                                                                | 2016<br>(2Q3Q)                 | 2016<br>(4Q) | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026<br>-2030 | 2031<br>-2035 | 2036<br>-2040 | 2041<br>-2045 | 2046<br>-2047 |       |       |
|                                                                                                                                                | (in millions)                  |              |      |      |      |      |      |      |      |      |      |               |               |               |               |               |       |       |
| Exposures<br>Previously<br>Subject to the<br>Voided<br>Recovery Act:<br>PRHTA<br>(Transportation<br>revenue)                                   | \$0                            | \$33         | \$0  | \$36 | \$42 | \$28 | \$23 | \$18 | \$19 | \$21 | \$1  | \$26          | \$151         | \$227         | \$240         | \$45          | \$—   | \$910 |
| PREPA                                                                                                                                          | 0                              | 20           | 0    | 5    | 4    | 25   | 42   | 22   | 22   | 81   | 78   | 52            | 309           | 84            | 0             | —             | —     | 744   |
| PRASA                                                                                                                                          | —                              | 15           | —    | —    | —    | —    | —    | —    | —    | —    | 2    | 25            | 84            | —             | 2             | 92            | 168   | 388   |
| PRHTA<br>(Highway<br>revenue)                                                                                                                  | —                              | 19           | —    | 10   | 10   | 21   | 22   | 26   | 6    | 8    | 8    | 8             | 27            | 167           | 37            | —             | —     | 369   |
| PRCCDA                                                                                                                                         | —                              | 11           | —    | —    | —    | —    | —    | —    | —    | —    | —    | —             | 19            | 105           | 29            | —             | —     | 164   |
| Total                                                                                                                                          | 0                              | 98           | 0    | 51   | 56   | 74   | 87   | 66   | 47   | 110  | 89   | 111           | 590           | 583           | 308           | 137           | 168   | 2,575 |
| Exposures Not<br>Previously<br>Subject to the<br>Voided<br>Recovery Act:<br>Commonwealth<br>of Puerto Rico -<br>General<br>Obligation<br>Bonds | 0                              | 142          | 0    | 95   | 75   | 82   | 137  | 16   | 37   | 14   | 73   | 68            | 255           | 475           | 146           | —             | —     | 1,615 |
| MFA                                                                                                                                            | —                              | 55           | —    | 47   | 47   | 44   | 37   | 33   | 33   | 16   | 12   | 11            | 52            | —             | —             | —             | —     | 387   |
| COFINA                                                                                                                                         | 0                              | (1)          | 0    | (1)  | (1)  | (1)  | (1)  | (2)  | (2)  | 1    | 0    | (2)           | (6)           | 32            | 99            | 155           | —     | 270   |
| Puerto Rico<br>Public<br>Buildings<br>Authority                                                                                                | —                              | 8            | —    | 30   | —    | 5    | 10   | 12   | 0    | 7    | 0    | 8             | 52            | 40            | 16            | —             | —     | 188   |
| PRIFA                                                                                                                                          | —                              | —            | —    | —    | 2    | —    | —    | —    | —    | 2    | —    | —             | —             | —             | 10            | 4             | —     | 18    |
| University of<br>Puerto Rico                                                                                                                   | —                              | 0            | —    | 0    | 0    | 0    | 0    | 0    | 0    | 0    | 0    | 0             | 0             | 1             | —             | —             | —     | 1     |
| Total                                                                                                                                          | 0                              | 204          | 0    | 171  | 123  | 130  | 183  | 59   | 68   | 40   | 85   | 85            | 353           | 548           | 271           | 159           | —     | 2,479 |

|                                  |     |       |     |       |       |       |       |       |       |       |       |       |       |         |       |       |       |         |
|----------------------------------|-----|-------|-----|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|---------|-------|-------|-------|---------|
| Total net par for<br>Puerto Rico | \$0 | \$302 | \$0 | \$222 | \$179 | \$204 | \$270 | \$125 | \$115 | \$150 | \$174 | \$196 | \$943 | \$1,131 | \$579 | \$296 | \$168 | \$5,054 |
|----------------------------------|-----|-------|-----|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|---------|-------|-------|-------|---------|

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Amortization Schedule  
of Net Debt Service Outstanding of Puerto Rico  
As of March 31, 2016

|                                                                                                                                             | Scheduled Net Debt Service Amortization |              |              |       |       |       |       |       |       |       |       |       |               |               |               |               |               | Total   |
|---------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------|--------------|--------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|---------------|---------------|---------------|---------------|---------------|---------|
|                                                                                                                                             | 2016<br>(2Q)                            | 2016<br>(3Q) | 2016<br>(4Q) | 2017  | 2018  | 2019  | 2020  | 2021  | 2022  | 2023  | 2024  | 2025  | 2026<br>-2030 | 2031<br>-2035 | 2036<br>-2040 | 2041<br>-2045 | 2046<br>-2047 |         |
|                                                                                                                                             | (in millions)                           |              |              |       |       |       |       |       |       |       |       |       |               |               |               |               |               |         |
| Exposures<br>Previously<br>Subject to the<br>Voided Recovery<br>Act:<br>PRHTA<br>(Transportation<br>revenue)                                | \$0                                     | \$57         | \$—          | \$82  | \$86  | \$69  | \$63  | \$57  | \$57  | \$58  | \$37  | \$61  | \$309         | \$348         | \$288         | \$47          | \$—           | \$1,619 |
| PREPA                                                                                                                                       | 2                                       | 35           | 2            | 38    | 37    | 58    | 74    | 52    | 50    | 109   | 102   | 72    | 366           | 92            | 0             | —             | —             | 1,089   |
| PRASA                                                                                                                                       | —                                       | 25           | —            | 19    | 19    | 19    | 19    | 19    | 19    | 19    | 21    | 45    | 160           | 68            | 70            | 159           | 181           | 862     |
| PRHTA<br>(Highway<br>revenue)                                                                                                               | —                                       | 29           | —            | 29    | 29    | 39    | 39    | 42    | 20    | 21    | 21    | 21    | 88            | 203           | 39            | —             | —             | 620     |
| PRCCDA                                                                                                                                      | —                                       | 15           | —            | 7     | 7     | 7     | 7     | 7     | 7     | 7     | 7     | 7     | 51            | 127           | 30            | —             | —             | 286     |
| Total                                                                                                                                       | 2                                       | 161          | 2            | 175   | 178   | 192   | 202   | 177   | 153   | 214   | 188   | 206   | 974           | 838           | 427           | 206           | 181           | 4,476   |
| Exposures Not<br>Previously<br>Subject to the<br>Voided Recovery<br>Act:<br>Commonwealth<br>of Puerto Rico -<br>General<br>Obligation Bonds | 0                                       | 184          | —            | 171   | 146   | 150   | 201   | 72    | 93    | 69    | 127   | 117   | 459           | 605           | 161           | —             | —             | 2,555   |
| MFA                                                                                                                                         | —                                       | 64           | —            | 64    | 62    | 56    | 47    | 40    | 39    | 21    | 16    | 15    | 57            | —             | —             | —             | —             | 481     |
| COFINA                                                                                                                                      | 0                                       | 6            | —            | 13    | 13    | 13    | 13    | 13    | 13    | 16    | 15    | 12    | 68            | 103           | 164           | 170           | —             | 632     |
| Puerto Rico<br>Public Buildings<br>Authority                                                                                                | —                                       | 13           | —            | 39    | 8     | 12    | 18    | 20    | 6     | 14    | 6     | 14    | 72            | 49            | 17            | —             | —             | 288     |
| PRIFA                                                                                                                                       | —                                       | 0            | —            | 1     | 3     | 1     | 1     | 1     | 1     | 3     | 0     | 1     | 4             | 3             | 13            | 4             | —             | 36      |
| University of<br>Puerto Rico                                                                                                                | —                                       | 0            | —            | 0     | 0     | 0     | 0     | 0     | 0     | 0     | 0     | 0     | 0             | 1             | —             | —             | —             | 1       |
| Total                                                                                                                                       | 0                                       | 267          | —            | 288   | 232   | 232   | 280   | 146   | 152   | 123   | 164   | 159   | 660           | 761           | 355           | 174           | —             | 3,993   |
| Total net debt<br>service for Puerto<br>Rico                                                                                                | \$2                                     | \$428        | \$2          | \$463 | \$410 | \$424 | \$482 | \$323 | \$305 | \$337 | \$352 | \$365 | \$1,634       | \$1,599       | \$782         | \$380         | \$181         | \$8,469 |



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## Exposure to Residential Mortgage-Backed Securities

The tables below provide information on the risk ratings and certain other risk characteristics of the Company's financial guaranty insurance and credit derivative RMBS exposures as of March 31, 2016. U.S. RMBS exposures represent 2% of the total net par outstanding, and BIG U.S. RMBS represent 24% of total BIG net par outstanding. See Note 5, Expected Loss to be Paid, of the Financial Statements, for a discussion of expected losses to be paid on U.S. RMBS exposures.

## Distribution of U.S. RMBS by Rating and Type of Exposure as of March 31, 2016

| Ratings:        | Prime<br>First<br>Lien | Alt-A<br>First Lien | Option<br>ARMs | Subprime<br>First<br>Lien | Second<br>Lien | Total Net<br>Par<br>Outstanding |
|-----------------|------------------------|---------------------|----------------|---------------------------|----------------|---------------------------------|
|                 | (dollars in millions)  |                     |                |                           |                |                                 |
| AAA             | \$8                    | \$ 209              | \$ 17          | \$ 1,560                  | \$30           | \$ 1,825                        |
| AA              | 92                     | 316                 | 80             | 390                       | 70             | 948                             |
| A               | 1                      | —                   | 4              | 34                        | 1              | 39                              |
| BBB             | 76                     | 15                  | —              | 92                        | 0              | 183                             |
| BIG             | 248                    | 698                 | 135            | 1,229                     | 1,372          | 3,682                           |
| Total exposures | \$425                  | \$ 1,238            | \$ 235         | \$ 3,305                  | \$1,474        | \$ 6,677                        |

## Distribution of U.S. RMBS by Year Insured and Type of Exposure as of March 31, 2016

| Year<br>insured: | Prime<br>First<br>Lien | Alt-A<br>First Lien | Option<br>ARMs | Subprime<br>First<br>Lien | Second<br>Lien | Total Net<br>Par<br>Outstanding |
|------------------|------------------------|---------------------|----------------|---------------------------|----------------|---------------------------------|
|                  | (in millions)          |                     |                |                           |                |                                 |
| 2004 and prior   | \$52                   | \$ 53               | \$ 17          | \$ 1,032                  | \$97           | \$ 1,252                        |
| 2005             | 121                    | 433                 | 35             | 173                       | 322            | 1,085                           |
| 2006             | 82                     | 189                 | 33             | 695                       | 412            | 1,411                           |
| 2007             | 169                    | 562                 | 150            | 1,337                     | 642            | 2,861                           |
| 2008             | —                      | —                   | —              | 67                        | —              | 67                              |
| Total exposures  | \$425                  | \$ 1,238            | \$ 235         | \$ 3,305                  | \$1,474        | \$ 6,677                        |

## Exposures by Reinsurer

Ceded par outstanding represents the portion of insured risk ceded to other reinsurers. Under these relationships, the Company cedes a portion of its insured risk in exchange for a premium paid to the reinsurer. The Company remains primarily liable for all risks it directly underwrites and is required to pay all gross claims. It then seeks reimbursement from the reinsurer for its proportionate share of claims. The Company may be exposed to risk for this exposure if it were required to pay the gross claims and not be able to collect ceded claims from an assuming company experiencing financial distress. A number of the financial guaranty insurers to which the Company has ceded par have experienced financial distress and as a result have been downgraded by the rating agencies. In addition, state insurance regulators have intervened with respect to some of these insurers.

In accordance with U.S. statutory accounting requirements and U.S. insurance laws and regulations, in order for the Company to receive credit for liabilities ceded to reinsurers domiciled outside of the U.S., such reinsurers must secure their liabilities to the Company. All of the unauthorized reinsurers in the table below are required to post collateral for

the benefit of the Company in an amount at least equal to the sum of their ceded unearned premium reserve, loss reserves and contingency reserves, all calculated on a statutory basis of accounting. In addition, certain authorized reinsurers in the table below post collateral on terms negotiated with the Company. Collateral may be in the form of letters of credit or trust accounts. The total collateral posted by all non-affiliated reinsurers as of March 31, 2016 was approximately \$436 million.

Assumed par outstanding represents the amount of par assumed by the Company from other monolines. Under these relationships, the Company assumes a portion of the ceding company's insured risk in exchange for a premium. The Company



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may be exposed to risk in this portfolio in that the Company may be required to pay losses without a corresponding premium in circumstances where the ceding company is experiencing financial distress and is unable to pay premiums.

In addition to assumed and ceded reinsurance arrangements, the Company may also have exposure to financial guaranty insurers in "second-to-pay" transactions, where the Company provides insurance on an obligation that is already insured by another financial guarantor. In that case, if the underlying obligor and the financial guarantor both fail to pay an amount scheduled to be paid, the Company would be obligated to pay. The Company underwrites these transactions based on the underlying obligation, without regard to the financial obligor. See Note 13, Reinsurance and Other Monoline Exposures, of the Financial Statements

## Exposure by Reinsurer

| Reinsurer                                                         | Ratings at<br>May 3, 2016      |                            | Par Outstanding (1)<br>As of March 31, 2016 |                                          |                            |
|-------------------------------------------------------------------|--------------------------------|----------------------------|---------------------------------------------|------------------------------------------|----------------------------|
|                                                                   | Moody's<br>Reinsurer<br>Rating | S&P<br>Reinsurer<br>Rating | Ceded Pay<br>Outstanding                    | Second-to-<br>Pay Insured<br>Outstanding | Assumed Par<br>Outstanding |
| (dollars in millions)                                             |                                |                            |                                             |                                          |                            |
| American Overseas Reinsurance Company Limited (2)                 | WR (3)                         | WR                         | \$4,960                                     | \$ —                                     | \$ 30                      |
| Tokio Marine & Nichido Fire Insurance Co., Ltd. (2)               | Aa3 (4)                        | A+ (4)                     | 4,171                                       | —                                        | —                          |
| Syncora Guarantee Inc. (2)                                        | WR                             | WR                         | 2,411                                       | 1,319                                    | 700                        |
| Mitsui Sumitomo Insurance Co. Ltd. (2)                            | A1                             | A+ (4)                     | 1,718                                       | —                                        | —                          |
| ACA Financial Guaranty Corp.                                      | NR (5)                         | WR                         | 700                                         | 38                                       | —                          |
| Ambac Assurance Corporation                                       | WR                             | WR                         | 117                                         | 3,892                                    | 9,589                      |
| National Public Finance Guarantee Corporation ("National")<br>(6) | A3                             | AA-                        | —                                           | 5,139                                    | 5,065                      |
| MBIA                                                              | (7)                            | (7)                        | —                                           | 1,591                                    | 428                        |
| FGIC                                                              | (8)                            | (8)                        | —                                           | 1,437                                    | 636                        |
| Ambac Assurance Corp. Segregated Account                          | NR                             | NR                         | —                                           | 86                                       | 823                        |
| CIFG Assurance North America Inc.                                 | WR                             | WR                         | —                                           | 43                                       | 2,784                      |
| Other (2)                                                         | Various                        | Various                    | 76                                          | 776                                      | 128                        |
| Total                                                             |                                |                            | \$14,153                                    | \$ 14,321                                | \$ 20,183                  |

(1) Includes par related to insured credit derivatives.

(2) The total collateral posted by all non-affiliated reinsurers required or agreeing to post collateral as of March 31, 2016 was approximately \$436 million.

(3) Represents "Withdrawn Rating."

(4) The Company benefits from trust arrangements that satisfy the triple-A credit requirement of S&P and/or Moody's.

(5) Represents "Not Rated."

(6) Rated AA+ by KBRA.

- (7) MBIA includes subsidiaries MBIA Insurance Corp. rated B by S&P and B3 by Moody's and MBIA U.K. Insurance Ltd. rated BB by S&P and Ba2 by Moody's.
- (8) FGIC includes subsidiaries Financial Guaranty Insurance Company and FGIC UK Limited both of which had their ratings withdrawn by rating agencies.

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As of March 31, 2016

| Reinsurer                                       | Internal Credit Rating |         |         |         |         | Total    |
|-------------------------------------------------|------------------------|---------|---------|---------|---------|----------|
|                                                 | AAA                    | AA      | A       | BBB     | BIG     |          |
|                                                 | (in millions)          |         |         |         |         |          |
| American Overseas Reinsurance Company Limited   | \$378                  | \$1,760 | \$1,528 | \$976   | \$318   | \$4,960  |
| Tokio Marine & Nichido Fire Insurance Co., Ltd. | 543                    | 522     | 1,126   | 1,358   | 622     | 4,171    |
| Syncora Guarantee Inc.                          | —                      | 132     | 422     | 1,734   | 123     | 2,411    |
| Mitsui Sumitomo Insurance Co. Ltd.              | 131                    | 504     | 551     | 359     | 173     | 1,718    |
| ACA Financial Guaranty Corp.                    | —                      | 449     | 240     | 11      | —       | 700      |
| Ambac Assurance Corporation                     | —                      | —       | 117     | —       | —       | 117      |
| Other                                           | 47                     | 0       | 1       | 28      | —       | 76       |
| Total                                           | \$1,099                | \$3,367 | \$3,985 | \$4,466 | \$1,236 | \$14,153 |

## Second-to-Pay

## Insured Par Outstanding by Internal Rating

As of March 31, 2016(1)

|                                          | Public Finance |       |       |       |       | Structured Finance |     |     |     |       |         |
|------------------------------------------|----------------|-------|-------|-------|-------|--------------------|-----|-----|-----|-------|---------|
|                                          | AAAAA          | A     | BBB   | BIG   | AAA   | AA                 | A   | BBB | BIG | Total |         |
|                                          | (in millions)  |       |       |       |       |                    |     |     |     |       |         |
| Syncora Guarantee Inc.                   | \$—            | \$71  | \$239 | \$617 | \$348 | \$—                | \$— | \$— | \$— | \$44  | \$1,319 |
| ACA Financial Guaranty Corp.             | —              | —     | 2     | 19    | 17    | —                  | —   | —   | —   | —     | 38      |
| Ambac Assurance Corporation              | 10             | 1,037 | 1,449 | 1,187 | 47    | 1                  | —   | 57  | 96  | 8     | 3,892   |
| National                                 | 71             | 1,655 | 3,387 | 1     | —     | —                  | —   | 25  | —   | —     | 5,139   |
| MBIA                                     | —              | 65    | 247   | 265   | —     | —                  | 750 | 81  | 80  | 103   | 1,591   |
| FGIC                                     | —              | 30    | 741   | 261   | 227   | 139                | —   | 5   | —   | 34    | 1,437   |
| Ambac Assurance Corp. Segregated Account | —              | —     | —     | —     | —     | —                  | 22  | —   | —   | 64    | 86      |
| CIFG Assurance North America Inc.        | —              | —     | —     | 22    | 21    | —                  | —   | —   | —   | —     | 43      |
| Other                                    | —              | 776   | —     | —     | —     | —                  | —   | —   | —   | —     | 776     |

|       |      |         |         |         |       |       |       |       |       |       |          |
|-------|------|---------|---------|---------|-------|-------|-------|-------|-------|-------|----------|
| Total | \$81 | \$3,634 | \$6,065 | \$2,372 | \$660 | \$140 | \$772 | \$168 | \$176 | \$253 | \$14,321 |
|-------|------|---------|---------|---------|-------|-------|-------|-------|-------|-------|----------|

(1) Assured Guaranty's internal rating.

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## Selected European Exposure

The European countries where the Company has exposure and believes heightened uncertainties exist are: Hungary, Italy, Portugal and Spain (collectively, the “Selected European Countries”). 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 tables, both gross and net of ceded reinsurance.

Gross Direct Economic Exposure  
to Selected European Countries(1)  
As of March 31, 2016

|                           | Hungary       | Italy   | Portugal | Spain | Total   |
|---------------------------|---------------|---------|----------|-------|---------|
|                           | (in millions) |         |          |       |         |
| Sub-sovereign exposure(2) | \$274         | \$1,082 | \$ 90    | \$470 | \$1,916 |
| Non-sovereign exposure(3) | 185           | 506     | —        | —     | 691     |
| Total                     | \$459         | \$1,588 | \$ 90    | \$470 | \$2,607 |
| Total BIG                 | \$385         | \$—     | \$ 90    | \$470 | \$945   |

Net Direct Economic Exposure  
to Selected European Countries(1)  
As of March 31, 2016

|                           | Hungary       | Italy   | Portugal | Spain | Total   |
|---------------------------|---------------|---------|----------|-------|---------|
|                           | (in millions) |         |          |       |         |
| Sub-sovereign exposure(2) | \$271         | \$827   | \$ 84    | \$375 | \$1,557 |
| Non-sovereign exposure(3) | 179           | 458     | —        | —     | 637     |
| Total                     | \$450         | \$1,285 | \$ 84    | \$375 | \$2,194 |
| Total BIG                 | \$379         | \$—     | \$ 84    | \$375 | \$838   |

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

Sub-sovereign exposure in Selected European Countries includes transactions backed by receivables from or (2) 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 and RMBS.

The tables above include the par amount of financial guaranty contracts accounted for as derivatives of \$116 million with a fair value of \$3 million, net of reinsurance. The Company’s credit derivative transactions are governed by International Swaps and Derivatives Association, Inc. ("ISDA") documentation, and the Company is required to make a loss payment on them only upon the occurrence of one or more defined credit events with respect to the referenced securities or loans.

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 \$206 million to Selected European Countries (plus Greece) in transactions with \$4.1 billion of net par outstanding. The indirect exposure to credits with a nexus to Greece is \$6 million across several highly rated pooled corporate obligations with net par outstanding of \$231 million.

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## Liquidity and Capital Resources

## Liquidity Requirements and Sources

## AGL and its Holding Company Subsidiaries

The liquidity of AGL, Assured Guaranty US Holdings Inc. ("AGUS") and Assured Guaranty Municipal Holdings Inc. ("AGMH") is largely dependent on dividends from their operating subsidiaries and their access to external financing. The liquidity requirements of these entities include the payment of operating expenses, interest on debt issued by AGUS and AGMH, and dividends on AGL's common shares. AGL and its holding company subsidiaries may also require liquidity to make periodic capital investments in their operating subsidiaries or, in the case of AGL, to repurchase its common shares pursuant to its share repurchase authorization. In the ordinary course of business, the Company evaluates its liquidity needs and capital resources in light of holding company expenses and dividend policy, as well as rating agency considerations. The Company also subjects its cash flow projections and its assets to a stress test, maintaining a liquid asset balance of one time its stressed operating company net cash flows. Management believes that AGL will have sufficient liquidity to satisfy its needs over the next twelve months. See "—Insurance Company Regulatory Restrictions" below for a discussion of the dividend restrictions of its insurance company subsidiaries.

## AGL and Holding Company Subsidiaries

## Significant Cash Flow Items

|                                          | First<br>Quarter<br>2016<br>(in<br>millions) |
|------------------------------------------|----------------------------------------------|
| Dividends paid by AGC to AGUS            | \$—\$ 20                                     |
| Dividends paid by AGM to AGMH            | 95 66                                        |
| Dividends paid by AG Re to AGL           | 25 50                                        |
| Repayment of surplus note by AGM to AGMH | — 25                                         |
| Dividends paid to AGL shareholders       | (18) (19 )                                   |
| Repurchases of common shares(1)          | (75) (152)                                   |
| Interest paid                            | (7) (7 )                                     |
| Issuance of note by AGUS to AGC(2)       | — (200)                                      |

(1) On February 24, 2016, in continuation of the Company's capital management strategy of repurchasing its common shares, the Company's Board of Directors approved the repurchase of a \$250 million of common shares. As of March 31, 2016 and May 4, 2016, on a settlement date basis, the remaining authorization for share repurchases was \$230 million and \$210 million, respectively.

(2) On March 31, 2015, AGUS, as lender, provided \$200 million to AGC, as borrower, from available funds to help partially fund the purchase of Radian Asset. AGC repaid that loan in full on April 14, 2015.

## Dividends From Subsidiaries

The Company anticipates that for the next twelve months, amounts paid by AGL's direct and indirect insurance company subsidiaries as dividends or other distributions will be a major source of its liquidity. The insurance company subsidiaries' ability to pay dividends depends upon their financial condition, results of operations, cash

requirements, and compliance with rating agency requirements, and is also subject to restrictions contained in the insurance laws and related regulations of their states of domicile. Dividend restrictions applicable to AGC and AGM, and to AG Re, are described under Note 11, Insurance Company Regulatory Requirements of the Financial Statements.

Under New York insurance law, AGM may only pay dividends out of "earned surplus," which is the portion of the company's surplus that represents the net earnings, gains or profits (after deduction of all losses) that have not been distributed to shareholders as dividends or transferred to stated capital or capital surplus, or applied to other purposes permitted by law, but does not include unrealized appreciation of assets. AGM may pay dividends without the prior approval of the New York Superintendent that, together with all dividends declared or distributed by it during the preceding 12 months, does not exceed the lesser of 10% of its policyholders' surplus



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(as of its last annual or quarterly statement filed with the New York Superintendent) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGM to distribute as dividends without regulatory approval is estimated to be approximately \$236 million, of which approximately \$32 million is estimated to be available for distribution in the second quarter of 2016.

Under Maryland's insurance law, AGC may, with prior notice to the Maryland Insurance Commissioner, pay an ordinary dividend that, together with all dividends paid in the prior 12 months, does not exceed the lesser of 10% of its policyholders' surplus (as of the prior December 31) or 100% of its adjusted net investment income during that period. The maximum amount available during 2016 for AGC to distribute as ordinary dividends will be approximately \$79 million, of which approximately \$24 million is available for distribution in the second quarter of 2016.

Municipal Assurance Corp. ("MAC") is a New York domiciled insurance company subject to the same dividend limitations described above for AGM. The Company does not currently anticipate that MAC will distribute any dividends.

For AG Re, any distribution (including repurchase of shares) of any share capital, contributed surplus or other statutory capital that would reduce its total statutory capital by 15% or more of its total statutory capital as set out in its previous year's financial statements requires the prior approval of the Bermuda Monetary Authority ("Authority"). Separately, dividends are paid out of an insurer's statutory surplus and cannot exceed that surplus. Further, annual dividends cannot exceed 25% of total statutory capital and surplus as set out in its previous year's financial statements, which is \$246 million, without AG Re certifying to the Authority that it will continue to meet required margins. Based on the foregoing limitations, in 2016 AG Re has the capacity to (i) make capital distributions in an aggregate amount up to \$127 million without the prior approval of the Authority and (ii) declare and pay dividends in an aggregate amount up to the limit of its outstanding statutory surplus, which is \$140 million. Such dividend capacity is further limited by the actual amount of AG Re's unencumbered assets, which amount changes from time to time due in part to collateral posting requirements. As of March 31, 2016, AG Re had unencumbered assets of approximately \$594 million.

Generally, dividends paid by a U.S. company to a Bermuda holding company are subject to a 30% withholding tax. After AGL became tax resident in the U.K., it became subject to the tax rules applicable to companies resident in the U.K., including the benefits afforded by the U.K.'s tax treaties. The income tax treaty between the U.K. and the U.S. reduces or eliminates the U.S. withholding tax on certain U.S. sourced investment income (to 5% or 0%), including dividends from U.S. subsidiaries to U.K. resident persons entitled to the benefits of the treaty.

## External Financing

From time to time, AGL and its subsidiaries have sought external debt or equity financing in order to meet their obligations. External sources of financing may or may not be available to the Company, and if available, the cost of such financing may not be acceptable to the Company.

## Intercompany Loans and Guarantees

On March 30, 2015, AGUS loaned \$200 million to AGC to facilitate the acquisition of Radian Asset on April 1, 2015. AGC repaid the loan in full on April 14, 2015.

From time to time, AGL and its subsidiaries have entered into intercompany loan facilities. For example, on October 25, 2013, AGL, as borrower, and AGUS, as lender, entered into a revolving credit facility pursuant to which AGL may, from time to time, borrow for general corporate purposes. Under the credit facility, AGUS committed to lend a

principal amount not exceeding \$225 million in the aggregate. Such commitment terminates on October 25, 2018 (the “loan termination date”). The unpaid principal amount of each loan will bear interest at a fixed rate equal to 100% of the then applicable Federal short-term or mid-term interest rate, as the case may be, as determined under Internal Revenue Code Sec. 1274(d), and interest on all loans will be computed for the actual number of days elapsed on the basis of a year consisting of 360 days. Accrued interest on all loans will be paid on the last day of each June and December, beginning on December 31, 2013, and at maturity. AGL must repay the then unpaid principal amounts of the loans by the third anniversary of the loan termination date. No amounts are currently outstanding under the credit facility.

In addition, in 2012 AGUS borrowed \$90 million from its affiliate Assured Guaranty Re Overseas Ltd. to fund the acquisition of MAC. That loan remained outstanding as of March 31, 2016.

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Furthermore, AGL fully and unconditionally guarantees the payment of the principal of, and interest on, the \$1,130 million aggregate principal amount of senior notes issued by AGUS and AGMH, and the \$450 million aggregate principal amount of junior subordinated debentures issued by AGUS and AGMH, in each case, as described under "Commitments and Contingencies -- Long-Term Debt Obligations " below.

Cash and Investments

As of March 31, 2016, AGL had \$80 million in cash and short-term investments. AGUS and AGMH had a total of \$42 million in cash and short-term investments. In addition, the Company's U.S. holding companies have \$70 million in fixed-maturity securities with weighted average duration of 0.4 years.

Insurance Company Subsidiaries

Liquidity of the insurance company subsidiaries is primarily used to pay for:

- operating expenses,
- claims on the insured portfolio,
- posting of collateral in connection with credit derivatives and reinsurance transactions,
- reinsurance premiums,
- dividends to AGL, AGUS and/or AGMH, as applicable,
- principal of and, where applicable, interest on surplus notes, and
- capital investments in their own subsidiaries, where appropriate.

Management believes that its subsidiaries' liquidity needs for the next twelve months can be met from current cash, short-term investments and operating cash flow, including premium collections and coupon payments as well as scheduled maturities and paydowns from their respective investment portfolios. The Company targets a balance of its most liquid assets including cash and short-term securities, Treasuries, agency RMBS and pre-refunded municipal bonds equal to 1.5 times its projected operating company cash flow needs over the next four quarters. The Company intends to hold and has the ability to hold temporarily impaired debt securities until the date of anticipated recovery.

Beyond the next twelve months, the ability of the operating subsidiaries to declare and pay dividends may be influenced by a variety of factors, including market conditions, insurance regulations and rating agency capital requirements and general economic conditions.

Insurance policies issued provide, in general, that payments of principal, interest and other amounts insured may not be accelerated by the holder of the obligation. Amounts paid by the Company therefore are typically in accordance with the obligation's original payment schedule, unless the Company accelerates such payment schedule, at its sole option.

Payments made in settlement of the Company's obligations arising from its insured portfolio may, and often do, vary significantly from year-to-year, depending primarily on the frequency and severity of payment defaults and whether the Company chooses to accelerate its payment obligations in order to mitigate future losses.

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## Claims (Paid) Recovered

|                                                             | First Quarter |        |
|-------------------------------------------------------------|---------------|--------|
|                                                             | 2016          | 2015   |
|                                                             | (in millions) |        |
| Public finance                                              | \$(5 )        | \$(2 ) |
| Structured finance:                                         |               |        |
| U.S. RMBS before benefit for recoveries for breaches of R&W | (98 )         | (39 )  |
| Net benefit for recoveries for breaches of R&W              | 13            | 21     |
| U.S. RMBS after benefit for recoveries for breaches of R&W  | (85 )         | (18 )  |
| Other structured finance                                    | (23 )         | 8      |
| Structured finance                                          | (108 )        | (10 )  |
| Claims (paid) recovered, net of reinsurance(1)              | \$(113)       | \$(12) |

(1) Includes \$8 million paid and \$6 million paid for consolidated FG VIEs for First Quarter 2016 and 2015, respectively.

As of March 31, 2016, the Company had exposure of approximately \$561 million to an infrastructure transaction with refinancing risk. The Company may be required to make claim payments on such exposure, the aggregate amount of the claim payments may be substantial and, although the Company may not experience ultimate loss on it, reimbursement may not occur for an extended time. This transaction involves a long-term infrastructure project that was financed by bonds that mature prior to the expiration of the project concession. The Company expects the cash flows from the project to be sufficient to repay all of the debt over the life of the project concession, and also expects the debt to be refinanced in the market at or prior to its maturity. If the issuer is unable to refinance the debt due to market conditions, the Company may have to pay a claim when the debt matures, and then recover from cash flows produced by the project in the future. The Company generally projects that in most scenarios it will be fully reimbursed for such claim payments. However, the recovery of such amounts is uncertain and may take from 10 to 35 years, depending on the performance of the underlying collateral. As of March 31, 2016, the Company estimated that total claims for the one transaction with significant refinancing risk, assuming no refinancing and based on certain performance assumptions, could be \$561 million on a gross basis; such claims would occur from 2018 through 2022.

In addition, the Company has net par exposure of \$5.1 billion to Commonwealth of Puerto Rico transactions, all of which are BIG. Puerto Rico has experienced significant general fund budget deficits in recent years. These deficits have been covered primarily with the net proceeds of bond issuances, with interim financings provided by GDB and, in some cases, with one-time revenue measures or expense adjustment measures. In addition to high debt levels, Puerto Rico faces a challenging economic environment. Information regarding the Company's exposure to the Commonwealth of Puerto Rico and its related authorities and public corporations is set forth in "Insured Portfolio-Exposure to Puerto Rico" above.

The terms of the Company's CDS contracts generally are modified from standard CDS contract forms approved by ISDA in order to provide for payments on a scheduled basis and to replicate the terms of a traditional financial guaranty insurance policy. Some contracts the Company entered into as the credit protection seller, however, utilize standard ISDA settlement mechanics of cash settlement (i.e., a process to value the loss of market value of a reference obligation) or physical settlement (i.e., delivery of the reference obligation against payment of principal by the protection seller) in the event of a "credit event," as defined in the relevant contract. Cash settlement or physical settlement generally requires the payment of a larger amount, prior to the maturity of the reference obligation, than would settlement on a "pay-as-you-go" basis, under which the Company would be required to pay scheduled interest shortfalls during the term of the reference obligation and scheduled principal shortfall only at the final maturity of the reference obligation. As of March 31, 2016, the Company was posting approximately \$308 million to secure its

obligations under CDS. Of that amount, approximately \$285 million related to \$3.5 billion in CDS gross par insured where the amount of required collateral is capped and the remaining \$23 million related to \$219 million in CDS gross par insured where the amount of required collateral is based on movements in the mark-to-market valuation of the underlying exposure.

On April 12, 2016, AGC entered into an agreement and plan of merger to acquire CIFG, the parent of financial guaranty insurer CIFG NA. AGC expects to pay \$450 million in cash to acquire CIFG, subject to adjustments as contemplated in the agreement, and the acquisition is expected to be completed mid-2016, subject to receipt of anti-trust and insurance regulatory approvals as well as satisfaction of customary closing conditions. CIFG's stockholders have already approved the acquisition. As part of the transaction, CIFG NA will merge into AGC, which will be the surviving entity. As of December 31,

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2015, CIFG had a consolidated insured portfolio of \$5.6 billion of net par and approximately \$637 million of consolidated qualified statutory capital.

## Consolidated Cash Flows

## Consolidated Cash Flow Summary

|                                                                                                                          | First Quarter<br>2016 2015<br>(in millions) |        |
|--------------------------------------------------------------------------------------------------------------------------|---------------------------------------------|--------|
| Net cash flows provided by (used in) operating activities before effects of trading securities and FG VIEs consolidation | \$(96 )                                     | \$8    |
| (Purchases) sales of trading securities, net                                                                             | —                                           | (3 )   |
| Effect of FG VIEs consolidation                                                                                          | 6                                           | 18     |
| Net cash flows provided by (used in) operating activities - reported                                                     | (90 )                                       | 23     |
| Net cash flows provided by (used in) investing activities before effects of FG VIEs consolidation                        | 136                                         | 980    |
| Effect of FG VIEs consolidation                                                                                          | 36                                          | 21     |
| Net cash flows provided by (used in) investing activities - reported                                                     | 172                                         | 1,001  |
| Net cash flows provided by (used in) financing activities before effects of FG VIEs consolidation                        | (94 )                                       | (173 ) |
| Effect of FG VIEs consolidation                                                                                          | (42 )                                       | (39 )  |
| Net cash flows provided by (used in) financing activities - reported (1)                                                 | (136 )                                      | (212 ) |
| Effect of exchange rate changes                                                                                          | 0                                           | (2 )   |
| Cash at beginning of period                                                                                              | 166                                         | 75     |
| Total cash at the end of the period                                                                                      | \$112                                       | \$885  |

(1) Claims paid on consolidated FG VIEs are presented in the consolidated cash flow statements as a component of paydowns on FG VIE liabilities in financing activities as opposed to operating activities.

Excluding net cash flows from purchases and sales of the trading portfolio and the effect of consolidating FG VIEs, cash inflows from operating activities decreased in First Quarter 2016 compared with First Quarter 2015 due primarily to acceleration of claim payments as a means of mitigating future losses, which were partially offset by lower taxes.

Investing activities were primarily net sales (purchases) of fixed-maturity and short-term investment securities. Investing cash flows in First Quarter 2016 and First Quarter 2015 include inflows of \$66 million and \$30 million for FG VIEs, respectively. In First Quarter 2015, the Company sold securities to fund the acquisition of Radian Asset by AGC.

Financing activities consisted primarily of paydowns of FG VIE liabilities and share repurchases. Financing cash flows in First Quarter 2016 and First Quarter 2015 include outflows of \$42 million and \$39 million for FG VIEs, respectively. Share repurchases in First Quarter 2016 and 2015 were \$75 million and \$152 million, respectively.

From April 1, 2016 through May 4, 2016, the Company repurchased an additional 0.8 million shares for \$20 million. As of March 31, 2016 and May 4, 2016, the Company had remaining authorization to purchase common shares of \$230 million and \$210 million, respectively, on a settlement basis. For more information about the Company's share repurchase authorization and the amounts it repurchased in 2016, see Note 17, Shareholders' Equity, of the Financial Statements.

## Commitments and Contingencies

## Leases

AGL and its subsidiaries lease office space and certain other items. Future cash payments associated with contractual obligations pursuant to operating leases for office space have not materially changed since December 31, 2015.

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## Long-Term Debt Obligations

The outstanding principal and interest paid on long-term debt were as follows:

Principal Outstanding  
and Interest Paid on Long-Term Debt

|                                                     | Principal Amount                               |                                  | Interest Paid            |      |
|-----------------------------------------------------|------------------------------------------------|----------------------------------|--------------------------|------|
|                                                     | As of<br>March<br>31,<br>2016<br>(in millions) | As of<br>December<br>31,<br>2015 | First<br>Quarter<br>2016 | 2015 |
| AGUS:                                               |                                                |                                  |                          |      |
| 7% Senior Notes(1)                                  | \$200                                          | \$ 200                           | \$ —                     | \$ — |
| 5% Senior Notes(1)                                  | 500                                            | 500                              | —                        | —    |
| Series A Enhanced Junior Subordinated Debentures(2) | 150                                            | 150                              | —                        | —    |
| Total AGUS                                          | 850                                            | 850                              | —                        | —    |
| AGMH(3):                                            |                                                |                                  |                          |      |
| 67/8% QUIBS(1)                                      | 100                                            | 100                              | 2                        | 2    |
| 6.25% Notes(1)                                      | 230                                            | 230                              | 4                        | 4    |
| 5.6% Notes(1)                                       | 100                                            | 100                              | 1                        | 1    |
| Junior Subordinated Debentures(2)                   | 300                                            | 300                              | —                        | —    |
| Total AGMH                                          | 730                                            | 730                              | 7                        | 7    |
| AGM(3):                                             |                                                |                                  |                          |      |
| AGM Notes Payable                                   | 11                                             | 12                               | 0                        | 0    |
| Total AGM                                           | 11                                             | 12                               | 0                        | 0    |
| Total                                               | \$1,591                                        | \$ 1,592                         | \$ 7                     | \$ 7 |

(1) AGL fully and unconditionally guarantees these obligations

(2) Guaranteed by AGL on a junior subordinated basis.

(3) Principal amounts vary from carrying amounts due primarily to acquisition method fair value adjustments at the AGMH acquisition date, which are accreted or amortized into interest expense over the remaining terms of these obligations.

7% Senior Notes issued by AGUS. On May 18, 2004, AGUS issued \$200 million of 7% senior notes due 2034 for net proceeds of \$197 million. Although the coupon on the Senior Notes is 7%, the effective rate is approximately 6.4%, taking into account the effect of a cash flow hedge.

5% Senior Notes issued by AGUS. On June 20, 2014, AGUS issued \$500 million of 5% Senior Notes due 2024 for net proceeds of \$495 million. The notes are guaranteed by AGL. The net proceeds from the sale of the notes were used for general corporate purposes, including the purchase of common shares of AGL.

Series A Enhanced Junior Subordinated Debentures issued by AGUS. On December 20, 2006, AGUS issued \$150 million of Debentures due 2066. The Debentures pay a fixed 6.4% rate of interest until December 15, 2016, and thereafter pay a floating rate of interest, reset quarterly, at a rate equal to three month London Interbank Offered Rate



("LIBOR") plus a margin equal to 2.38%. AGUS may select at one or more times to defer payment of interest for one or more consecutive periods for up to ten years. Any unpaid interest bears interest at the then applicable rate. AGUS may not defer interest past the maturity date.

6 7/8% QUIBS issued by AGMH. On December 19, 2001, AGMH issued \$100 million face amount of 6 7/8% QUIBS due December 15, 2101, which are callable without premium or penalty.

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6.25% Notes issued by AGMH. On November 26, 2002, AGMH issued \$230 million face amount of 6.25% Notes due November 1, 2102, which are callable without premium or penalty in whole or in part.

5.6% Notes issued by AGMH. On July 31, 2003, AGMH issued \$100 million face amount of 5.6% Notes due July 15, 2103, which are callable without premium or penalty in whole or in part.

Junior Subordinated Debentures issued by AGMH. On November 22, 2006, AGMH issued \$300 million face amount of Junior Subordinated Debentures with a scheduled maturity date of December 15, 2036 and a final repayment date of December 15, 2066. The final repayment date of December 15, 2066 may be automatically extended up to four times in five-year increments provided certain conditions are met. The debentures are redeemable, in whole or in part, at any time prior to December 15, 2036 at their principal amount plus accrued and unpaid interest to the date of redemption or, if greater, the make-whole redemption price. Interest on the debentures will accrue from November 22, 2006 to December 15, 2036 at the annual rate of 6.4%. If any amount of the debentures remains outstanding after December 15, 2036, then the principal amount of the outstanding debentures will bear interest at a floating interest rate equal to one-month LIBOR plus 2.215% until repaid. AGMH may elect at one or more times to defer payment of interest on the debentures for one or more consecutive interest periods that do not exceed ten years. In connection with the completion of this offering, AGMH entered into a replacement capital covenant for the benefit of persons that buy, hold or sell a specified series of AGMH long-term indebtedness ranking senior to the debentures. Under the covenant, the debentures will not be repaid, redeemed, repurchased or defeased by AGMH or any of its subsidiaries on or before the date that is twenty years prior to the final repayment date, except to the extent that AGMH has received proceeds from the sale of replacement capital securities. The proceeds from this offering were used to pay a dividend to the shareholders of AGMH.

## Recourse Credit Facility

In connection with the acquisition of AGMH, AGM agreed to retain the risks relating to the debt and strip policy portions of the leveraged lease business. The liquidity risk to AGM related to the strip policy portion of the leveraged lease business is mitigated by the strip coverage facility described below.

In a leveraged lease transaction, a tax-exempt entity (such as a transit agency) transfers tax benefits to a tax-paying entity by transferring ownership of a depreciable asset, such as subway cars. The tax-exempt entity then leases the asset back from its new owner.

If the lease is terminated early, the tax-exempt entity must make an early termination payment to the lessor. A portion of this early termination payment is funded from monies that were pre-funded and invested at the closing of the leveraged lease transaction (along with earnings on those invested funds). The tax-exempt entity is obligated to pay the remaining, unfunded portion of this early termination payment (known as the “strip coverage”) from its own sources. AGM issued financial guaranty insurance policies (known as “strip policies”) that guaranteed the payment of these unfunded strip coverage amounts to the lessor, in the event that a tax-exempt entity defaulted on its obligation to pay this portion of its early termination payment. AGM can then seek reimbursement of its strip policy payments from the tax-exempt entity, and can also sell the transferred depreciable asset and reimburse itself from the sale proceeds.

Currently, all the leveraged lease transactions in which AGM acts as strip coverage provider are breaching a rating trigger related to AGM and are subject to early termination. However, early termination of a lease does not result in a draw on the AGM policy if the tax-exempt entity makes the required termination payment. If all the leases were to terminate early and the tax-exempt entities do not make the required early termination payments, then AGM would be exposed to possible liquidity claims on gross exposure of approximately \$1.1 billion as of March 31, 2016. To date, none of the leveraged lease transactions that involve AGM has experienced an early termination due to a lease default and a claim on the AGM policy. It is difficult to determine the probability that AGM will have to pay strip provider

claims or the likely aggregate amount of such claims. At March 31, 2016, approximately \$1.4 billion of cumulative strip par exposure had been terminated since 2008 on a consensual basis. The consensual terminations have resulted in no claims on AGM.

On July 1, 2009, AGM and Dexia Crédit Local S.A., acting through its New York Branch (“Dexia Crédit Local (NY)”), entered into a credit facility (the “Strip Coverage Facility”). Under the Strip Coverage Facility, Dexia Crédit Local (NY) agreed to make loans to AGM to finance all draws made by lessors on AGM strip policies that were outstanding as of November 13, 2008, up to the commitment amount, which is currently \$495 million.

Fundings under this facility are subject to certain conditions precedent, and their repayment is collateralized by a security interest that AGM granted to Dexia Crédit Local (NY) in amounts that AGM recovers – from the tax-exempt entity, or from asset sale proceeds – following its payment of strip policy claims. On June 30, 2014, AGM and Dexia Crédit Local (NY)

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agreed to shorten the duration of the facility. Accordingly, the Strip Coverage Facility will terminate upon the earliest to occur of an AGM change of control, the reduction of the commitment amount to \$0 in accordance with the terms of the facility, and June 30, 2024 (rather than the original maturity date of January 31, 2042).

The Strip Coverage Facility's financial covenants require that AGM and its subsidiaries maintain:

- a maximum debt-to-capital ratio of 30%; and

- a minimum net worth of 75% of consolidated net worth as of July 1, 2009, plus, beginning June 30, 2015 and on each anniversary of such date, an amount equal to the product of (i) 25% of the aggregate consolidated net income (or loss) for the period beginning July 2, 2009 and ending on June 30, 2014 and (ii) a fraction, the numerator of which is the commitment amount as of the relevant calculation date and the denominator of which is \$1 billion.

The Company was in compliance with all financial covenants as of March 31, 2016.

The Strip Coverage Facility contains restrictions on AGM, including, among other things, in respect of its ability to incur debt, permit liens, pay dividends or make distributions, dissolve or become party to a merger or consolidation. Most of these restrictions are subject to exceptions. The Strip Coverage Facility has customary events of default, including (subject to certain materiality thresholds and grace periods) payment default, bankruptcy or insolvency proceedings and cross-default to other debt agreements.

As of March 31, 2016, no amounts were outstanding under this facility, nor have there been any borrowings during the life of this facility.

### Committed Capital Securities

Each of AGC and AGM have issued \$200 million of CCS pursuant to transactions in which AGC CCS or AGM's Committed Preferred Trust Securities (the "AGM CPS"), as applicable, were issued by custodial trusts created for the primary purpose of issuing such securities, investing the proceeds in high-quality assets and providing put options to AGC or AGM, as applicable. The put options allow AGC and AGM to issue non-cumulative redeemable perpetual preferred securities to the trusts in exchange for cash. For both AGC and AGM, four initial trusts were created, each with an initial aggregate face amount of \$50 million. The Company does not consider itself to be the primary beneficiary of the trusts for either the AGC or AGM CCS and the trusts are not consolidated in Assured Guaranty's financial statements.

The trusts provide AGC and AGM access to new capital at their respective sole discretion through the exercise of the put options. Upon AGC's or AGM's exercise of its put option, the relevant trust will liquidate its portfolio of eligible assets and use the proceeds to purchase the AGC or AGM preferred stock, as applicable. AGC or AGM may use the proceeds from such sale of its preferred stock to the trusts for any purpose, including the payment of claims. The put agreements have no scheduled termination date or maturity. However, each put agreement will terminate if (subject to certain grace periods) specified events occur.

**AGC Committed Capital Securities.** AGC entered into separate put agreements with four custodial trusts with respect to its CCS in April 2005. The AGC put options have not been exercised through the date of this filing. Initially, all of AGC CCS were issued to a special purpose pass-through trust (the "Pass-Through Trust"). The Pass-Through Trust was dissolved in April 2008 and the AGC CCS were distributed to the holders of the Pass-Through Trust's securities. Neither the Pass-Through Trust nor the custodial trusts are consolidated in the Company's financial statements. Income distributions on the Pass-Through Trust securities and CCS were equal to an annualized rate of one-month LIBOR plus 110 basis points for all periods ending on or prior to April 8, 2008.

Following dissolution of the Pass-Through Trust, distributions on the AGC CCS are determined pursuant to an auction process. On April 7, 2008 this auction process failed, thereby increasing the annualized rate on the AGC CCS to one-month LIBOR plus 250 basis points. Distributions on the AGC preferred stock will be determined pursuant to the same process. AGC continues to have the ability to exercise its put option and cause the related trusts to purchase AGC Preferred Stock.

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AGM Committed Capital Securities. AGM entered into separate put agreements with four custodial trusts with respect to its CCS in June 2003. The AGM put options have not been exercised through the date of this filing. AGM pays a floating put premium to the trusts, which represents the difference between the commercial paper yield and the winning auction rate (plus all fees and expenses of the trust). If an auction does not attract sufficient clearing bids, however, the auction rate is subject to a maximum rate of one-month LIBOR plus 200 basis points for the next succeeding distribution period. Beginning in August 2007, the AGM CCS required the maximum rate for each of the relevant trusts. AGM continues to have the ability to exercise its put option and cause the related trusts to purchase AGM Preferred Stock.

## Investment Portfolio

The Company's principal objectives in managing its investment portfolio are to support the highest possible ratings for each operating company; to manage investment risk within the context of the underlying portfolio of insurance risk; to maintain sufficient liquidity to cover unexpected stress in the insurance portfolio; and to maximize after-tax net investment income.

The Company's fixed-maturity securities and short-term investments had a duration of 5.3 years as of March 31, 2016 and 5.4 years as of December 31, 2015. Generally, the Company's fixed-maturity securities are designated as available-for-sale. For more information about the Investment Portfolio and a detailed description of the Company's valuation of investments see Note 10, Investments and Cash, of the Financial Statements.

Fixed-Maturity Securities and Short-Term Investments  
by Security Type

|                                                 | As of March 31,<br>2016 |                         | As of December 31,<br>2015 |                         |
|-------------------------------------------------|-------------------------|-------------------------|----------------------------|-------------------------|
|                                                 | Amortized<br>Cost       | Estimated<br>Fair Value | Amortized<br>Cost          | Estimated<br>Fair Value |
|                                                 | (in millions)           |                         |                            |                         |
| Fixed-maturity securities:                      |                         |                         |                            |                         |
| Obligations of state and political subdivisions | \$5,417                 | \$ 5,776                | \$5,528                    | \$ 5,841                |
| U.S. government and agencies                    | 379                     | 405                     | 377                        | 400                     |
| Corporate securities                            | 1,473                   | 1,525                   | 1,505                      | 1,520                   |
| Mortgage-backed securities(1):                  |                         |                         |                            |                         |
| RMBS                                            | 1,222                   | 1,239                   | 1,238                      | 1,245                   |
| CMBS                                            | 531                     | 556                     | 506                        | 513                     |
| Asset-backed securities                         | 821                     | 811                     | 831                        | 825                     |
| Foreign government securities                   | 280                     | 276                     | 290                        | 283                     |
| Total fixed-maturity securities                 | 10,123                  | 10,588                  | 10,275                     | 10,627                  |
| Short-term investments                          | 459                     | 459                     | 396                        | 396                     |
| Total fixed-maturity and short-term investments | \$10,582                | \$ 11,047               | \$10,671                   | \$ 11,023               |

(1) Government-agency obligations were approximately 52% of mortgage backed securities as of March 31, 2016 and 54% as of December 31, 2015, based on fair value.

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The following tables summarize, for all fixed-maturity securities in an unrealized loss position as of March 31, 2016 and December 31, 2015, the aggregate fair value and gross unrealized loss by length of time the amounts have continuously been in an unrealized loss position.

## Fixed-Maturity Securities

## Gross Unrealized Loss by Length of Time

As of March 31, 2016

|                                                           | Less than 12 months   |                 | 12 months or more |                 | Total      |                 |
|-----------------------------------------------------------|-----------------------|-----------------|-------------------|-----------------|------------|-----------------|
|                                                           | Fair Value            | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |
|                                                           | (dollars in millions) |                 |                   |                 |            |                 |
| Obligations of state and political subdivisions           | \$58                  | \$ 0            | \$ 87             | \$ (1 )         | \$145      | \$ (1 )         |
| U.S. government and agencies                              | 7                     | 0               | —                 | —               | 7          | 0               |
| Corporate securities                                      | 78                    | (2 )            | 122               | (15 )           | 200        | (17 )           |
| Mortgage-backed securities:                               |                       |                 |                   |                 |            |                 |
| RMBS                                                      | 123                   | (5 )            | 182               | (15 )           | 305        | (20 )           |
| CMBS                                                      | 7                     | 0               | 5                 | 0               | 12         | 0               |
| Asset-backed securities                                   | 456                   | (13 )           | —                 | —               | 456        | (13 )           |
| Foreign government securities                             | 91                    | (4 )            | 53                | (5 )            | 144        | (9 )            |
| Total                                                     | \$820                 | \$ (24 )        | \$ 449            | \$ (36 )        | \$1,269    | \$ (60 )        |
| Number of securities(1)                                   |                       | 110             |                   | 82              |            | 185             |
| Number of securities with other-than-temporary impairment |                       | 12              |                   | 6               |            | 18              |

## Fixed-Maturity Securities

## Gross Unrealized Loss by Length of Time

As of December 31, 2015

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

(1) The number of securities does not add across because lots of the same securities have been purchased at different times and appear in both categories above (i.e. Less than 12 months and 12 months or more). If a security appears

in both categories, it is counted only once in the total column.



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Of the securities in an unrealized loss position for 12 months or more as of March 31, 2016, eleven securities had an unrealized loss greater than 10% of book value. The total unrealized loss for these securities as of March 31, 2016 was \$26 million. The Company has determined that the unrealized losses recorded as of March 31, 2016 are yield related and not the result of other-than-temporary impairment.

Changes in interest rates affect the value of the Company's fixed-maturity portfolio. As interest rates fall, the fair value of fixed-maturity securities generally increases and as interest rates rise, the fair value of fixed-maturity securities generally decreases. The Company's portfolio of fixed-maturity securities consists primarily of high-quality, liquid instruments.

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

Distribution of Fixed-Maturity Securities  
by Contractual Maturity  
As of March 31, 2016

|                                       | Amortized<br>Cost | Estimated<br>Fair Value |
|---------------------------------------|-------------------|-------------------------|
|                                       | (in millions)     |                         |
| Due within one year                   | \$469             | \$ 470                  |
| Due after one year through five years | 1,654             | 1,719                   |
| Due after five years through 10 years | 2,195             | 2,320                   |
| Due after 10 years                    | 4,052             | 4,284                   |
| Mortgage-backed securities:           |                   |                         |
| RMBS                                  | 1,222             | 1,239                   |
| CMBS                                  | 531               | 556                     |
| Total                                 | \$ 10,123         | \$ 10,588               |

The following table summarizes the ratings distributions of the Company's investment portfolio as of March 31, 2016 and December 31, 2015. Ratings reflect the lower of the Moody's and S&P classifications, except for bonds purchased for loss mitigation or other risk management strategies, which use Assured Guaranty's internal ratings classifications.

Distribution of  
Fixed-Maturity Securities by Rating

| Rating    | As of<br>March<br>31,<br>2016 | As of<br>December<br>31, 2015 |
|-----------|-------------------------------|-------------------------------|
| AAA       | 11.4 %                        | 10.8 %                        |
| AA        | 58.6                          | 59.0                          |
| A         | 17.3                          | 17.6                          |
| BBB       | 1.0                           | 0.9                           |
| BIG(1)    | 11.4                          | 11.4                          |
| Not rated | 0.3                           | 0.3                           |
| Total     | 100.0 %                       | 100.0 %                       |

- (1) Comprised primarily of loss mitigation and other risk management assets. See Note 10, Investments and Cash, of the Financial Statements.

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

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statutory and regulatory requirements in the amount of \$1,550 million and \$1,411 million as of March 31, 2016 and December 31, 2015, respectively, based on fair value.

The fair value of the Company's pledged securities to secure its obligations under its CDS exposure totaled \$308 million and \$305 million as of March 31, 2016 and December 31, 2015, respectively.

### Liquidity Arrangements with respect to AGMH's former Financial Products Business

AGMH's former financial products segment had been in the business of borrowing funds through the issuance of guaranteed investment contracts ("GICs") and medium term notes and reinvesting the proceeds in investments that met AGMH's investment criteria. The financial products business also included the equity payment undertaking agreement portion of the leveraged lease business, as described further below in "—Leveraged Lease Business."

### The GIC Business

Until November 2008, AGMH, through its financial products business, offered GICs to municipalities and other market participants. The GICs were issued through certain non-insurance subsidiaries of AGMH. In return for an initial payment, each GIC entitles its holder to receive the return of the holder's invested principal plus interest at a specified rate, and to withdraw principal from the GIC as permitted by its terms. AGM insures the payment obligations on all these GICs.

The proceeds of GICs were loaned to AGMH's former subsidiary FSA Asset Management LLC ("FSAM"). FSAM in turn invested these funds in fixed-income obligations (the "FSAM assets").

AGM's insurance policies on the GICs remain in place, and must remain in place until each GIC is terminated, even though AGMH no longer holds any ownership interest in FSAM or the GIC issuers.

In June 2009, in connection with the Company's acquisition of AGMH from Dexia Holdings Inc., Dexia SA, the ultimate parent of Dexia Holdings Inc., and certain of its affiliates, entered into a number of agreements intended to mitigate the credit, interest rate and liquidity risks associated with the GIC business and the related AGM insurance policies. Some of those agreements have since terminated or expired, or been modified. In addition to the surviving agreements described below, AGM benefits from a guaranty jointly and severally issued by Dexia SA and Dexia Crédit Local S.A. to AGM that guarantees the payment obligations of AGM under its insurance policies related to the GIC business, and an indemnification agreement between AGM, Dexia SA and Dexia Crédit Local S.A. that protects AGM from other losses arising out of or as a result of the GIC business.

To support the primary payment obligations under the GICs, each of Dexia SA and Dexia Crédit Local S.A. are party to a put contract. Pursuant to the put contract, FSAM may put an amount of its FSAM assets to Dexia SA and Dexia Crédit Local S.A. in exchange for funds that FSAM would in turn make available to meet demands for payment under the GICs. The amount that could be put varies depending on the type of trigger event in question. To secure their obligations under this put contract, Dexia SA and Dexia Crédit Local S.A. are required to post eligible highly liquid collateral having an aggregate value (subject to agreed reductions and advance rates) equal to at least the excess of (i) the aggregate principal amount of all outstanding GICs over (ii) the aggregate mark-to-market value of FSAM's assets.

As of March 31, 2016, approximately 31.6% of the FSAM assets (measured by aggregate principal balance) were in cash or were obligations backed by the full faith and credit of the United States.

As of March 31, 2016, the aggregate accreted GIC balance was approximately \$1.7 billion, compared with approximately \$10.2 billion as of December 31, 2009. As of March 31, 2016, and with respect to the FSAM assets, the aggregate accreted principal was approximately \$2.5 billion, the aggregate market value was approximately \$2.3 billion and the aggregate market value after agreed reductions was approximately \$1.6 billion. Cash and positive derivative value exceeded the negative derivative values and other projected costs by approximately \$161 million. Accordingly, as of March 31, 2016, the aggregate fair market value of the assets supporting the GIC business (disregarding the agreed upon reductions) plus cash and positive derivative value exceeded by nearly \$0.8 billion the aggregate principal amount of all outstanding GICs and certain other business and hedging costs of the GIC business. Even after applying the agreed upon reductions to the fair market value of the assets, the aggregate value of the assets supporting the GIC business plus cash and positive derivative value exceeded the aggregate principal amount of all outstanding GICs and certain other business and hedging costs of the GIC business. Accordingly, no posting of collateral was required under the primary put contract.

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To provide additional support, Dexia Crédit Local S.A. provides a liquidity commitment to FSAM to lend against FSAM assets under a revolving credit agreement. As of March 31, 2016 the commitment totaled \$1.3 billion, of which approximately \$0.8 billion was drawn. The agreement requires the commitment remain in place, generally until the GICs have been paid in full.

Despite the put contract and revolving credit agreement, and the significant portion of FSAM assets comprised of highly liquid securities backed by the full faith and credit of the United States, AGM remains subject to the risk that Dexia SA and its affiliates may not make payments or securities available (i) on a timely basis, which is referred to as “liquidity risk,” or (ii) at all, which is referred to as “credit risk,” because of the risk of default. Even if the Dexia entities have sufficient assets to pay all amounts when due (either under the GICs, or under the guarantee, the put contract and the revolving credit agreement), one or more rating agencies may view negatively the ability or willingness of Dexia SA and its affiliates to perform under their various agreements, which could negatively affect AGM’s ratings.

If Dexia SA or its affiliates do not fulfill their contractual obligations, the GIC issuers may not have the financial ability to pay upon the withdrawal of GIC funds or post collateral or make other payments in respect of the GICs, thereby resulting in claims upon the AGM financial guaranty insurance policies. If AGM is required to pay a claim due to a failure of the GIC issuers to pay amounts in respect of the GICs, AGM is subject to the risk that the GICs will not be paid from funds received from Dexia SA and its affiliates before it is required to make payment under its financial guaranty policies or that it will not receive the guaranty payment at all.

A downgrade of the financial strength rating of AGM could trigger a payment obligation of AGM in respect to AGMH's former GIC business. Most of the GICs insured by AGM allow for the withdrawal of GIC funds in the event of a downgrade of AGM, unless the relevant GIC issuer posts collateral or otherwise enhances its credit. Most GICs insured by AGM allow for the termination of the GIC contract and a withdrawal of GIC funds at the option of the GIC holder in the event of a downgrade of AGM below a specified threshold, generally below A- by S&P or A3 by Moody's, with no right of the GIC issuer to avoid such withdrawal by posting collateral or otherwise enhancing its credit. Each GIC contract stipulates the thresholds below which the GIC issuer must post eligible collateral, along with the types of securities eligible for posting and the collateralization percentage applicable to each security type. These collateralization percentages range from 100% of the GIC balance for cash posted as collateral to, typically, 108% for asset-backed securities. FSAM is expected to have sufficient eligible and liquid assets to satisfy any expected withdrawal and collateral posting obligations resulting from future rating actions affecting AGM.

## The Medium Term Notes Business

In connection with the acquisition of AGMH, Dexia Crédit Local S.A. agreed to fund, on behalf of AGM, 100% of all policy claims made under financial guaranty insurance policies issued by AGM in relation to the medium term notes issuance program of FSA Global Funding Limited. Such agreement is set out in a Separation Agreement, dated as of July 1, 2009, between Dexia Crédit Local S.A., AGM, FSA Global Funding and Premier International Funding Co., and in a funding guaranty and a reimbursement guaranty that Dexia Crédit Local S.A. issued for the benefit of AGM. Under the funding guaranty, Dexia Crédit Local S.A. guarantees to pay to or on behalf of AGM amounts equal to the payments required to be made under policies issued by AGM relating to the medium term notes business. Under the reimbursement guaranty, Dexia Crédit Local S.A. guarantees to pay reimbursement amounts to AGM for payments it makes following a claim for payment under an obligation insured by a policy it has issued. Notwithstanding Dexia Crédit Local S.A.’s obligation to fund 100% of all policy claims under those policies, AGM has a separate obligation to remit to Dexia Crédit Local S.A. a certain percentage (ranging from 0% to 25%) of those policy claims. AGM, the Company and related parties are also protected against losses arising out of or as a result of the medium term note business through an indemnification agreement with Dexia Crédit Local S.A. As of March 31, 2016, FSA Global Funding Limited had approximately \$705 million of medium term notes outstanding.

#### Leveraged Lease Business

Under the Strip Coverage Facility entered into in connection with the acquisition of AGMH, Dexia Credit Local (NY) agreed to make loans to AGM to finance all draws made by lessors on certain AGM strip policies issued in connection with the leveraged lease business. AGM may request advances under the Strip Coverage Facility without any explicit limit on the number of loan requests, provided that the aggregate principal amount of loans outstanding as of the date of the request may not exceed the commitment amount. The leveraged lease business, the AGM strip policies and the Strip Coverage Facility (including the commitment amount) are described further under "Commitments and Contingencies-Recourse Credit Facility" above.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for an updated sensitivity analysis for credit derivatives and expected losses on contracts accounted for as insurance. There were no material changes in market risk since December 31, 2015.

ITEM 4. CONTROLS AND PROCEDURES

Assured Guaranty’s management, with the participation of AGL’s President and Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) that are effective in recording, processing, summarizing and reporting, within the time periods specified in the Securities and Exchange Commission’s rules and forms, information required to be disclosed by AGL in the reports that it files or submits under the Exchange Act and ensuring that such information is accumulated and communicated to management, including the President and Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

Management of the Company, with the participation of its Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company’s disclosure controls and procedures as of March 31, 2016. Based on their evaluation as of March 31, 2016 covered by this Form 10-Q, the Company’s Chief Executive Officer and Chief Financial Officer have concluded that the Company’s disclosure controls and procedures were effective.

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### PART II. OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS

The Company is subject to legal proceedings and claims, as described in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, and in Note 14 to the Consolidated Financial Statements, Commitments and Contingencies – Legal Proceedings. During the three months ended March 31, 2016, the following developments occurred in respect of the Company's legal proceedings:

On November 28, 2011, Lehman Brothers International (Europe) (in administration) ("LBIE") sued AG Financial Products Inc. ("AGFP"), an affiliate of AGC which in the past had provided credit protection to counterparties under credit default swaps. AGC acts as the credit support provider of AGFP under these credit default swaps. LBIE's complaint, which was filed in the Supreme Court of the State of New York, alleged that AGFP improperly terminated nine credit derivative transactions between LBIE and AGFP and improperly calculated the termination payment in connection with the termination of 28 other credit derivative transactions between LBIE and AGFP. Following defaults by LBIE, AGFP properly terminated the transactions in question in compliance with the agreement between AGFP and LBIE, and calculated the termination payment properly. AGFP calculated that LBIE owes AGFP approximately \$29 million in connection with the termination of the credit derivative transactions, whereas LBIE asserted in the complaint that AGFP owes LBIE a termination payment of approximately \$1.4 billion. On February 3, 2012, AGFP filed a motion to dismiss certain of the counts in the complaint, and on March 15, 2013, the court granted AGFP's motion to dismiss the count relating to improper termination of the nine credit derivative transactions and denied AGFP's motion to dismiss the counts relating to the remaining transactions. On February 22, 2016, AGFP filed a motion for summary judgment on the remaining causes of action asserted by LBIE and on AGFP's counterclaims. LBIE's administrators disclosed in an April 10, 2015 report to LBIE's unsecured creditors that LBIE's valuation expert has calculated LBIE's damages in aggregate for the 28 transactions to range between a minimum of approximately \$200 million and a maximum of approximately \$500 million, depending on what adjustment, if any, is made for AGFP's credit risk and excluding any applicable interest. Notwithstanding the range calculated by LBIE's valuation expert, the Company cannot reasonably estimate the possible loss, if any, that may arise from this lawsuit.

On May 28, 2014, Houston Casualty Company Europe, Seguros y Reseguros, S.A. ("HCCE") notified Radian Asset that it was demanding arbitration against Radian Asset in connection with housing cooperative losses presented to Radian Asset by HCCE under several years of quota-share surety reinsurance contracts. Through November 30, 2015, HCCE had presented AGC, as successor to Radian Asset, with approximately €15 million in claims. In January 2016, Assured Guaranty and HCCE settled all the claims related to the Spanish housing cooperative losses.

During 2008, nine putative class action lawsuits were filed in federal court alleging federal antitrust violations in the municipal derivatives industry, seeking damages and alleging, among other things, a conspiracy to fix the pricing of, and manipulate bids for, municipal derivatives, including GICs. These cases have been coordinated and consolidated for pretrial proceedings in the U.S. District Court for the Southern District of New York as MDL 1950, In re Municipal Derivatives Antitrust Litigation, Case No. 1:08-cv-2516 ("MDL 1950"). On September 22, 2015, the remaining parties to the putative class action reported to the MDL 1950 Court that settlements in principle had been reached, and a motion for preliminary approval of those putative class claims was filed on February 24, 2016. The parties have reported that final settlement with those remaining defendants would resolve the putative class case. The settlement fairness hearing for those putative class cases is scheduled for July 8, 2016. The Company cannot reasonably estimate the possible loss, if any, or range of loss that may arise from these lawsuits.

#### ITEM 1A. RISK FACTORS



Please refer to "Risk Factors" under Part I, "Item 1A. Risk Factors" of the Company's Annual Report on Form 10-K for the year ended December 31, 2015. There have been no material changes to the risk factors disclosed in such Annual Report on Form 10-K during the three months ended March 31, 2016.

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## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

## Issuer's Purchases of Equity Securities

The following table reflects purchases of AGL common shares made by the Company during First Quarter 2016.

| Period                   | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price Paid<br>Per Share | Total Number of<br>Shares Purchased as<br>Part of Publicly<br>Announced Program<br>(1) | Maximum Number<br>(or Approximate<br>Dollar Value)<br>of Shares that<br>May Yet Be<br>Purchased<br>Under the Program(2) |
|--------------------------|-------------------------------------------|------------------------------------|----------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------|
| January 1 - January 31   | 1,776,387                                 | \$ 24.57                           | 1,776,387                                                                              | \$ 11,384,707                                                                                                           |
| February 1 - February 29 | 482,215                                   | \$ 23.61                           | 482,215                                                                                | \$ 250,000,000                                                                                                          |
| March 1 - March 31       | 780,326                                   | \$ 25.63                           | 780,326                                                                                | \$ 230,000,012                                                                                                          |
| Total                    | 3,038,928                                 | \$ 24.69                           | 3,038,928                                                                              |                                                                                                                         |

After giving effect to repurchases since the beginning of 2013 through May 4, 2016, the Company has repurchased a total of 61.7 common shares for approximately \$1,504 million, excluding commissions, at an average price of (1)\$24.36 per share. On February 24, 2016, the Company's Board of Directors approved a \$250 million share repurchase authorization. As of May 4, 2016, \$210 million of total capacity remained from the authorization, on a settlement basis.

(2)Excludes commissions.

## ITEM 6. EXHIBITS.

See Exhibit Index for a list of exhibits filed with this report.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

ASSURED GUARANTY LTD.  
(Registrant)

Dated May 5, 2016 By: /s/ ROBERT A. BAIENSON

Robert A. Bailenson  
Chief Financial Officer (Principal Financial and  
Accounting Officer and Duly Authorized Officer)

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EXHIBIT INDEX

| Exhibit<br>Number | Description of Document                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
|-------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 10.1              | Director Compensation Summary*                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| 10.2              | Agreement and Plan of Merger, dated as of April 12, 2016, among Assured Guaranty Corp., Cultivate Merger Sub, Inc. and CIFG Holding Inc.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
| 31.1              | Certification of CEO Pursuant to Exchange Act Rules 13A-14 and 15D-14, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| 31.2              | Certification of CFO Pursuant to Exchange Act Rules 13A-14 and 15D-14, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| 32.1              | Certification of CEO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| 32.2              | Certification of CFO Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| 101.1             | The following financial information from Assured Guaranty Ltd.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2015 formatted in XBRL: (i) Consolidated Balance Sheets at September 30, 2015 and December 31, 2014; (ii) Consolidated Statements of Operations for the Three and Nine Months ended September 30, 2015 and 2014; (iii) Consolidated Statements of Comprehensive Income for the Three and Nine Months ended September 30, 2015 and 2014 (iv) Consolidated Statement of Shareholders' Equity for the Nine Months ended September 30, 2015; (v) Consolidated Statements of Cash Flows for the Nine Months ended September 30, 2015 and 2014; and (vi) Notes to Consolidated Financial Statements. |

\* Management contract or compensatory plan