ASSURED GUARANTY LTD
Form 10-Q
August 09, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)
x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended June 30, 2012
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition Period from to
Commission File No. 001-32141
ASSURED GUARANTY LTD.
(Exact name of registrant as specified in its charter)

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

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

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

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

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

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

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

The number of registrant's Common Shares ($0.01 par value) outstanding as of August 1, 2012 was 194,067,746 (includes 88,549 unvested restricted shares).

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ASSURED GUARANTY LTD.

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ITEM 1. Financial Statements

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Assured Guaranty Ltd.

Consolidated Balance Sheets (unaudited)

(dollars in thousands except per share and share amounts)

	As of June 30, 2012	As of December 31, 2011
Assets		
Investment portfolio:		
Fixed maturity securities, available-for-sale, at fair value (amortized cost of $9,618,789 and $9,638,404)	$10,207,514	$10,141,850
Short term investments, at fair value	919,784	734,046
Other invested assets	194,447	222,869
Total investment portfolio	11,321,745	11,098,765
Cash	175,347	214,544
Premiums receivable, net of ceding commissions payable	964,063	1,002,852
Ceded unearned premium reserve	590,781	708,872
Deferred acquisition costs	126,755	132,418
Reinsurance recoverable on unpaid losses	170,495	69,300
Salvage and subrogation recoverable	376,760	367,718
Credit derivative assets	429,891	468,933
Deferred tax asset, net	815,084	803,529
Current income tax receivable	63,192	76,430
Financial guaranty variable interest entities' assets, at fair value	2,725,979	2,819,077
Other assets	314,372	262,222
Total assets	$18,074,464	$18,024,660
Liabilities and shareholders' equity		
Unearned premium reserve	$5,583,380	$5,962,799
Loss and loss adjustment expense reserve	995,217	679,011
Reinsurance balances payable, net	186,676	170,982
Long-term debt	846,354	1,038,302
Credit derivative liabilities	2,095,852	1,772,803
Financial guaranty variable interest entities' liabilities with recourse, at fair value	2,239,067	2,396,945
Financial guaranty variable interest entities' liabilities without recourse, at fair value	1,042,275	1,061,497
Other liabilities	361,577	290,756
Total liabilities	13,350,398	13,373,095
Commitments and contingencies (See Note 12)		
Common stock ($0.01 par value, 500,000,000 shares authorized; 193,956,481 and 182,235,798 shares issued and outstanding in 2012 and 2011)	1,939	1,822
Additional paid-in capital	2,719,988	2,569,922
Retained earnings	1,568,397	1,707,922
Accumulated other comprehensive income, net of tax of $159,679 and $135,344	429,342	367,499
Deferred equity compensation (320,193 shares in 2012 and 2011)	4,400	4,400
Total shareholders' equity	4,724,066	4,651,565
Total liabilities and shareholders' equity	$18,074,464	$18,024,660

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 thousands except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Revenues				
Net earned premiums	$219,299	$230,068	$412,976	$484,045
Net investment income	101,588	102,591	199,350	200,003
Net realized investment gains (losses):				
Other-than-temporary impairment losses	(9,042)	(26,818)	(36,386)	(33,765)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	(7,201)	(15,240)	(29,666)	(17,609)
Other net realized investment gains (losses)	(1,315)	6,488	4,880	13,872
Net realized investment gains (losses)	(3,156)	(5,090)	(1,840)	(2,284)
Net change in fair value of credit derivatives:				
Realized gains (losses) and other settlements	(22,664)	(10,836)	(79,545)	24,591
Net unrealized gains (losses)	283,327	(54,059)	(350,431)	(325,695)
Net change in fair value of credit derivatives	260,663	(64,895)	(429,976)	(301,104)
Fair value gain (loss) on committed capital securities	4,290	569	(9,614)	1,095
Fair value gains (losses) on financial guaranty variable interest entities	172,356	(174,286)	135,754	(54,685)
Other income	4,458	27,337	95,442	68,137
Total revenues	759,498	116,294	402,092	395,207
Expenses				
Loss and loss adjustment expenses	122,446	123,913	369,293	98,333
Amortization of deferred acquisition costs	4,526	5,810	9,939	9,472
Interest expense	25,426	24,696	50,099	49,456
Other operating expenses	53,447	53,249	114,727	116,132
Total expenses	205,845	207,668	544,058	273,393
Income (loss) before income taxes	553,653	(91,374)	(141,966)	121,814
Provision (benefit) for income taxes				
Current	(29,132)	9,864	396	(187,735)
Deferred	206,237	(58,133)	(35,886)	213,398
Total provision (benefit) for income taxes	177,105	(48,269)	(35,490)	25,663
Net income (loss)	$376,548	$(43,105)	$(106,476)	$96,151
Earnings per share:				
Basic	2.02	(0.23)	(0.58)	0.52
Diluted	2.01	(0.23)	(0.58)	0.51
Dividends per share	0.09	0.045	0.18	0.09

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 thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income (loss)	$376,548	$(43,105)	$(106,476)	$96,151
Unrealized holding gains (losses) arising during the period on:				
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $8,333, $61,394, $27,382 and $41,762	31,925	127,198	74,048	80,808
Investments with other-than-temporary impairment, net of tax provision (benefit) of $(1,141), $(5,323), $(8,486) and $3,872	(4,321)	(12,389)	(18,057)	8,456
Unrealized holding gains (losses) arising during the period, net of tax	27,604	114,809	55,991	89,264
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $(3,975), $(1,743), $(5,247), and $(1,571)	(4,637)	(4,227)	(5,493)	(3,198)
Change in net unrealized gains on investments	32,241	119,036	61,484	92,462
Change in cumulative translation adjustment, net of tax provision (benefit) of $(636), $191, $305 and $860	(1,182)	346	568	1,589
Change in cash flow hedge, net of tax provision (benefit) of $(57), $(57), $(113) and $(113)	(104)	(104)	(209)	(209)
Other comprehensive income (loss)	30,955	119,278	61,843	93,842
Comprehensive income (loss)	$407,503	$76,173	$(44,633)	$189,993

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

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Assured Guaranty Ltd.

Consolidated Statement of Shareholders' Equity (unaudited)

For the Six Months Ended, June 30, 2012

(dollars in thousands, except share data)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Deferred Equity Compensation	Total Shareholders' Equity
	Shares	Amount					
Balance at December 31, 2011	182,235,798	$1,822	$2,569,922	$1,707,922	$ 367,499	$ 4,400	$4,651,565
Net loss	—	—	—	(106,476)	—	—	(106,476)
Dividends ($0.18 per share)	—	—	—	(32,878)	—	—	(32,878)
Dividends on restricted stock units	—	—	171	(171)	—	—	—
Common stock issuance, net	13,428,770	134	172,366	—	—	—	172,500
Common stock repurchases	(2,066,759)	(21)	(24,292)	—	—	—	(24,313)
Share-based compensation and other	358,672	4	1,821	—	—	—	1,825
Other comprehensive income	—	—	—	—	61,843	—	61,843
Balance at June 30, 2012	193,956,481	$1,939	$2,719,988	$1,568,397	$ 429,342	$ 4,400	$4,724,066

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 thousands)

	Six Months Ended June 30,	
	2012	2011
Net cash flows provided by (used in) operating activities	$162,138	$631,946
Investing activities		
Fixed maturity securities:		
Purchases	(923,704)	(1,349,745)
Sales	525,523	685,980
Maturities	514,725	325,750
Net sales (purchases) of short-term investments	(108,014)	(49,901)
Net proceeds from paydowns on financial guaranty variable interest entities' assets	282,790	423,977
Acquisition of MIAC, net of cash acquired	(91,094)	—
Other	73,232	8,696
Net cash flows provided by (used in) investing activities	273,458	44,757
Financing activities		
Proceeds from issuances of common stock	172,500	—
Dividends paid	(32,878)	(16,577)
Repurchases of common stock	(24,313)	—
Share activity under option and incentive plans	(2,209)	(2,652)
Net paydowns of financial guaranty variable interest entities' liabilities	(388,576)	(593,294)
Repayment of long-term debt	(195,668)	(10,294)
Net cash flows provided by (used in) financing activities	(471,144)	(622,817)
Effect of exchange rate changes	(3,649)	3,215
Increase (decrease) in cash	(39,197)	57,101
Cash at beginning of period	214,544	108,389
Cash at end of period	$175,347	$165,490
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$(15,500)	$89,202
Interest	$46,787	$45,711

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

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Assured Guaranty Ltd.

Notes to Consolidated Financial Statements (Unaudited)

June 30, 2012

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, infrastructure and structured finance markets. The Company has applied its credit underwriting judgment, risk management skills and capital markets experience to offer insurance that protects holders of debt instruments and other monetary obligations from defaults in scheduled payments, including scheduled interest and principal payments. The securities insured by the Company include tax-exempt and taxable obligations issued by U.S. state or municipal governmental authorities, utility districts or facilities; notes or bonds issued to finance international infrastructure projects; and asset-backed securities that are generally issued by special purpose entities. The Company markets its credit protection products directly to issuers and underwriters of public finance, infrastructure and structured finance securities as well as to investors in such debt obligations. The Company guarantees debt obligations issued in many countries, although its principal focus is on the U.S., Europe and Australia.

Financial guaranty insurance policies provide an unconditional and irrevocable guaranty that protects the holder of a financial obligation against non-payment of principal and interest ("Debt Service") when due. Upon an obligor’s default on scheduled principal or interest payments due on the obligation, the Company is required under the financial guaranty policy to pay the principal or interest shortfall. The Company has issued financial guaranty insurance policies on both public finance obligations and structured finance obligations. Public finance obligations insured by the Company consist primarily of general obligation bonds supported by the issuers’ taxing powers, tax-supported bonds and revenue bonds and other obligations of states, their political subdivisions and other municipal issuers supported by the issuers’ or obligors’ covenant to impose and collect fees and charges for public services or specific projects. Public finance obligations include obligations backed by the cash flow from leases or other revenues from projects serving substantial public purposes, including government office buildings, toll roads, health care facilities and utilities. Structured finance obligations insured by the Company are generally issued by special purpose entities and backed by pools of assets such as residential or commercial mortgage loans, consumer or trade receivables, securities or other assets having an ascertainable cash flow or market value. The Company also insures other specialized financial obligations.

In the past, the Company had sold credit protection by issuing policies that guaranteed payment obligations under credit derivatives. 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 and only occurs upon one or more defined credit events such as failure to pay or bankruptcy, in each case, as defined within the transaction documents, with respect to one or more third party referenced securities or loans. Financial guaranty contracts accounted for as credit derivatives are primarily comprised of credit default swaps (“CDS”). 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 (the “Dodd-Frank Act”) also contributed to the decision of the Company not to enter into such new CDS in the foreseeable

future. The Company actively pursues opportunities to terminate existing CDS and, in certain cases, has converted existing CDS exposure into a financial guaranty insurance contract. These actions have the effect of reducing future fair value volatility in income and/or reducing rating agency capital charges.

The Company has historically entered into ceded reinsurance contracts in order to obtain greater business diversification and reduce the net potential loss from large risks. In January 2012, two of AGL's operating subsidiaries, Assured Guaranty Municipal Corp. (“AGM”) and Assured Guaranty Corp. (“AGC”), entered into a $435 million excess of loss reinsurance facility with third-party reinsurers, which reduced rating agency capital charges. The Company also has been reassuming previously ceded business from reinsurers. In the three-month period ended March 31, 2012 (“First Quarter 2012”), the Company reassumed a total of $19.1 billion in par from two reinsurers. See Note 11, Reinsurance and Other Monoline Exposures.

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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 nationally recognized statistical rating organizations ("NRSROs") 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 high financial strength ratings. However, the models used by NRSROs differ, presenting conflicting goals that may make it inefficient or impractical to reach the highest rating level. The models are not fully transparent, contain subjective data (such as assumptions about future market demand for the Company's products) and change frequently. Ratings reflect only the views of the respective NRSROs and are subject to continuous review and revision or withdrawal at any time.

Unless otherwise noted, ratings disclosed herein on Assured Guaranty's insured portfolio reflect Assured Guaranty's internal ratings. Assured Guaranty's ratings scale is similar to that used by the NRSROs; however, the ratings in these financial statements may not be the same as those assigned by any such rating agency. For example, the super senior category, which is not generally used by rating agencies, is used by Assured Guaranty in instances where Assured Guaranty's AAA-rated exposure on its internal rating scale (which does not take into account Assured Guaranty's financial guaranty) has additional credit enhancement due to either (1) the existence of another security rated AAA that is subordinated to Assured Guaranty's exposure or (2) Assured Guaranty's exposure benefiting from a different form of credit enhancement that would pay any claims first in the event that any of the exposures incurs a loss, and such credit enhancement, in management's opinion, causes Assured Guaranty's attachment point to be materially above the AAA attachment point.

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 financial guaranty variable interest entities ("FG VIEs") for the periods presented. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. These unaudited interim consolidated financial statements are as of June 30, 2012 and cover the three-month period ended June 30, 2012 ("Second Quarter, 2012"), the three-month period ended June 30, 2011 ("Second Quarter 2011"), the six-month period ended June 30, 2012 ("Six Months 2012") and the six-month period ended June 30, 2011 ("Six Months 2011"). The year-end balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP.

The unaudited interim consolidated financial statements include the accounts of AGL and its direct and indirect subsidiaries (collectively, the "Subsidiaries") and its consolidated FG 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, 2011, filed with the U.S. Securities and Exchange Commission (the "SEC").

AGL's principal insurance company subsidiaries are AGC, domiciled in Maryland; AGM, domiciled in New York; and Assured Guaranty Re Ltd. ("AG Re"), domiciled in Bermuda. In addition, the Company has another U.S. and another

Bermuda insurance company subsidiary that participate in a pooling agreement with AGM, two insurance subsidiaries organized in the United Kingdom, and a mortgage insurance company domiciled in New York. On May 31, 2012, the Company completed the purchase of Municipal and Infrastructure Assurance Corporation ("MIAC"), which is domiciled in New York. See Note 2. The Company's organizational structure includes various holdings companies, two of which—Assured Guaranty US Holdings Inc. ("AGUS") and Assured Guaranty Municipal Holdings Inc. ("AGMH")—have public debt outstanding. See Note 13, Long Term Debt and Credit Facilities.

2. Business Changes, Risks, Uncertainties and Accounting Developments

Summarized below are updates of the most significant recent events that have had, or may have in the future, a material effect on the financial position, results of operations or business prospects of the Company.

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Rating Actions

Standard and Poor's Ratings Services ("S&P") and Moody's Investors Service, Inc ("Moody's") have downgraded the financial strength ratings of all the Company's insurance subsidiaries over the course of the last several years. On March 20, 2012, Moody's placed the ratings of AGL and its Subsidiaries, including the insurance financial strength rating of the Company's insurance subsidiaries, other than the newly acquired MIAC subsidiary, on review for possible downgrade. There can be no assurance that S&P and Moody's will not take further action on the Company's ratings. See Note 4, Financial Guaranty Insurance Contracts, Note 6, Financial Guaranty Contracts Accounted for as Credit Derivatives and Note 11, Reinsurance and Other Monoline Exposure for more information regarding the effect of S&P and Moody's rating actions on the Company. See also Note 13, Long Term Debt and Credit Facilities for a discussion of the impact of a downgrade in the financial strength rating on the Company's insured leveraged lease transactions and Note 12, Commitments and Contingencies for a discussion of the impact of a downgrade in the financial strength rating on guaranteed investment contracts ("GICs") that AGM has insured. The insurance subsidiaries' financial strength ratings are an important competitive factor in the financial guaranty insurance and reinsurance markets. If the financial strength or financial enhancement ratings of the Company's insurance subsidiaries were reduced below current levels, the Company expects it could have adverse effects on its future business opportunities as well as the premiums it could charge for its insurance policies and consequently, a downgrade could harm the Company's new business production and results of operations in a material respect.

Accounting Changes

There has recently been significant GAAP rule making activity which has affected the accounting policies and presentation of the Company's financial information beginning on January 1, 2012, particularly:

· adoption of new guidance that restricted the types and amounts of financial guaranty insurance acquisition costs that may be deferred. See Note 4, Financial Guaranty Insurance Contracts.

· adoption of guidance that changed the presentation of other comprehensive income ("OCI"). See "Consolidated Statements of Comprehensive Income."

· adoption of guidance requiring additional fair value disclosures. See Note 5, Fair Value Measurement.

Deutsche Bank Agreement

On May 8, 2012, Assured Guaranty reached a settlement with Deutsche Bank AG and certain of its affiliates (collectively, "Deutsche Bank"), resolving claims related to certain residential mortgage-backed securities ("RMBS") transactions issued, underwritten or sponsored by Deutsche Bank that were insured by Assured Guaranty under financial guaranty insurance policies and to certain RMBS exposures in re-securitization transactions as to which Assured Guaranty provides credit protection through CDS. As part of the settlement agreement (the "Deutsche Bank Agreement"), Assured Guaranty settled its litigation against Deutsche Bank on three RMBS transactions.

Assured Guaranty received a cash payment of $165.6 million from Deutsche Bank upon signing of the Deutsche Bank Agreement, a portion of which partially reimbursed Assured Guaranty for past losses on certain transactions. Assured Guaranty and Deutsche Bank also entered into loss sharing arrangements covering future RMBS related losses, which are described below. Under the Deutsche Bank Agreement, Deutsche Bank AG placed approximately $282.7 million of eligible assets in trust in order to collateralize the obligations of a reinsurance affiliate under the loss-sharing arrangements, and the Deutsche Bank reinsurance affiliate may post additional collateral in the future to satisfy rating agency requirements.

The settlement includes eight RMBS transactions ("Covered Transactions") that Assured Guaranty has insured through financial guaranty insurance policies. The Covered Transactions are backed by first lien and second lien mortgage loans. Under the Deutsche Bank Agreement, the Deutsche Bank reinsurance affiliate will reimburse 80% of Assured Guaranty's future losses on the Covered Transactions until Assured Guaranty's aggregate losses (including those to date that are partially reimbursed by the $165.6 million cash payment) reach $318.8 million. Assured Guaranty currently projects that the Covered Transactions will not generate aggregate losses in excess of $318.8 million. In the event aggregate losses exceed $388.8 million, the Deutsche Bank reinsurance affiliate is required to resume reimbursement at the rate of 85% of Assured Guaranty's losses in excess of $388.8 million until such losses reach $600.0 million. The Covered Transactions represented $567.8 million of gross par outstanding as of June 30, 2012.

Certain uninsured tranches ("Uninsured Tranches") of three of the Covered Transactions are included as collateral in

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RMBS re- securitization transactions as to which Assured Guaranty provides credit protection through CDS. Under the Deutsche Bank Agreement, the Deutsche Bank reinsurance affiliate will reimburse losses on the CDS in an amount equal to 60% of losses in these Uninsured Tranches until the aggregate losses in the Uninsured Tranches reach $141.1 million. Assured Guaranty currently projects that the Uninsured Tranches will not generate losses in excess of $141.1 million in the base case scenario. In the event aggregate losses exceed $161.1 million, reimbursement resumes at the rate of 60% until the aggregate losses reach $185.1 million. The Deutsche Bank reinsurance affiliate is required to reimburse any losses in excess of $185.1 million at the rate of 100% until the aggregate losses reach $247.8 million. The Uninsured Tranches represent $329.3 million of par outstanding as of June 30, 2012.

Except for the Uninsured Tranches, the settlement does not include Assured Guaranty’s CDS with Deutsche Bank. The parties have agreed to continue efforts to resolve CDS-related claims.

Reinsurance Agreements

As discussed in Note 11, Reinsurance and Other Monoline Exposures, the Company has entered into several agreements with reinsurers, including assumption and re-assumption agreements with Radian Asset Assurance Inc. ("Radian"), a re-assumption agreement with Tokio Marine & Nichido Fire Insurance Co., Ltd. (“Tokio”) and a $435 million excess of loss reinsurance facility.

MIAC Acquisition

On May 31, 2012, the Company purchased 100% of the outstanding common stock of MIAC from Radian for $91.1 million in cash, resulting in $16.0 million in indefinite-lived intangible assets which represents the value of MIAC's licenses. Assets acquired consisted primarily of short-term investments. Investment income earned on these assets was not material for the Six Months 2012. MIAC is licensed to provide financial guaranty insurance and reinsurance in 38 U.S. jurisdictions including the District of Columbia. The acquisition of MIAC enhances the Company's flexibility to respond to changes in the financial guaranty industry.

Remarketing of Senior Notes and Redemption of Equity Units

On June 1, 2012, the Company completed the remarketing of the $172.5 million aggregate principal amount of 8.50% Senior Notes issued by AGUS in 2009 that were components of the Company's Equity Units; AGUS purchased all of the Senior Notes in the remarketing at a price of 100% of the aggregate principal amount thereof, and retired all of such notes on June 1, 2012. The proceeds from the remarketing were used to satisfy the obligations of the holders of the Equity Units to purchase AGL common shares pursuant to the forward purchase contracts that were also components of the Equity Units. Accordingly, on June 1, 2012, AGL issued 3.8924 common shares to holders of each $50 Equity Unit, which represented a settlement rate of 3.8685 common shares plus certain anti-dilution adjustments, or an aggregate of 13,428,770 common shares. The Equity Units ceased to exist when the forward purchase contracts were settled on June 1, 2012.

3. Outstanding Exposure

The Company’s financial guaranty contracts are written in different forms, but collectively are considered financial guaranty contracts. The Company seeks to limit its exposure to losses by underwriting obligations that are investment grade at inception, diversifying its portfolio and maintaining rigorous subordination or collateralization requirements on structured finance obligations. The Company also has utilized reinsurance by ceding business to third-party reinsurers. The Company provides financial guaranties with respect to debt obligations of special purpose entities, including VIEs. Some of these VIEs are consolidated as described in Note 7, Consolidation of Variable Interest Entities. The outstanding par and Debt Service amounts presented below include outstanding exposures on VIEs

whether or not they are consolidated.

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Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding	
	June 30, 2012	December 31, 2011	June 30, 2012	December 31, 2011
	(in millions)			
Public finance	$767,155	$798,471	$719,301	$716,890
Structured finance	123,437	137,661	115,787	128,775
Total financial guaranty	$890,592	$936,132	$835,088	$845,665

In addition to the amounts shown in the table above, the Company's net mortgage guaranty insurance in force was approximately $148 million as of June 30, 2012. The net mortgage guaranty insurance in force comprises $133 million covering loans originated in Ireland and $15 million covering loans originated in the UK.

Financial Guaranty Portfolio by Internal Rating

	As of June 30, 2012									
	Public Finance U.S.		Public Finance Non-U.S.		Structured Finance U.S		Structured Finance Non-U.S		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
	(dollars in millions)									
Super senior	$—	— %	$1,109	2.8 %	$15,157	18.2 %	$4,777	22.9 %	$21,043	3.8 %
AAA	4,771	1.2	1,388	3.6	32,947	39.5	9,225	44.2	48,331	8.7
AA	136,709	33.3	998	2.6	10,416	12.5	889	4.3	149,012	27.0
A	220,154	53.7	10,657	27.5	4,692	5.6	1,352	6.5	236,855	42.8
BBB	43,836	10.7	22,102	57.0	4,201	5.0	2,740	13.1	72,879	13.2
Below-investment-grade ("BIG")	4,407	1.1	2,515	6.5	16,017	19.2	1,875	9.0	24,814	4.5
Total net par outstanding	$409,877	100.0%	$38,769	100.0%	$83,430	100.0%	$20,858	100.0%	$552,934	100.0%

	As of December 31, 2011									
	Public Finance U.S.		Public Finance Non-U.S.		Structured Finance U.S		Structured Finance Non-U.S		Total	
Rating Category	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%	Net Par Outstanding	%
	(dollars in millions)									
Super senior	$—	— %	$1,138	2.9 %	$16,756	18.2 %	$5,660	23.9 %	$23,554	4.2 %
AAA	5,074	1.3	1,381	3.5	35,736	38.7	10,231	43.2	52,422	9.4
AA	139,693	34.6	1,056	2.7	12,575	13.6	976	4.1	154,300	27.7
A	213,164	52.9	11,744	30.1	4,115	4.5	1,518	6.4	230,541	41.3
BBB	40,635	10.1	21,399	54.8	5,044	5.5	3,391	14.3	70,469	12.6
BIG	4,507	1.1	2,328	6.0	18,008	19.5	1,919	8.1	26,762	4.8
Total net par outstanding	$403,073	100.0%	$39,046	100.0%	$92,234	100.0%	$23,695	100.0%	$558,048	100.0%

In First Quarter 2012, the Company reclassified to AA 80% of the net par outstanding of those first lien transactions that are covered by the Bank of America Agreement (see Note 4, Financial Guaranty Insurance Contracts) and that the Company otherwise internally rated below AA. The Company reclassified those amounts as AA exposure due to the eligible assets that Bank of America has placed into trust in order to collateralize its reimbursement obligation relating to such first lien transactions. This reclassification resulted in a decrease in BIG net par outstanding as of December 31, 2011 of $1,452 million from that previously reported.

In addition to amounts shown in the tables above, the Company had outstanding commitments to provide guaranties of

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$1.8 billion for structured finance and $0.5 billion for public finance obligations at June 30, 2012. The structured finance commitments include the unfunded component of pooled corporate and other transactions. Public finance commitments typically relate to primary and secondary public finance debt issuances. The expiration dates for the public finance commitments range between July 1, 2012 and February 25, 2017, with $0.2 billion expiring prior to December 31, 2012. The commitments are contingent on the satisfaction of all conditions set forth in them and may expire unused or be cancelled at the counterparty's request. Therefore, the total commitment amount does not necessarily reflect actual future guaranteed amounts.

Economic Exposure to the Selected European Countries

Several European countries are experiencing significant economic, fiscal and/or political strains such that the likelihood of default on obligations with a nexus to those countries may be higher than the Company anticipated when such factors did not exist. The Company is closely monitoring its exposures in European countries where it believes heightened uncertainties exist, specifically, Greece, Hungary, Ireland, Italy, Portugal and Spain (the "Selected European Countries"). Published reports have identified countries that may be experiencing reduced demand for their sovereign debt in the current environment. The Company selected these European countries based on these reports and its view that their credit fundamentals are deteriorating. The Company's 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.

Net Economic Exposure to Selected European Countries(1)
June 30, 2012

	Greece(2)	Hungary	Ireland	Italy	Portugal	Spain	Total
	(in millions)						
Sovereign and sub-sovereign exposure:							
Public finance	$276	$—	$—	$977	$110	$257	$1,620
Infrastructure finance	—	430	23	322	99	165	1,039
Sub-total	276	430	23	1,299	209	422	2,659
Non-sovereign exposure:							
Regulated utilities	—	—	—	222	—	12	234
RMBS	—	215	133	489	—	—	837
Commercial receivables	—	1	19	26	14	18	78
Pooled corporate	31	—	208	227	14	492	972
Sub-total	31	216	360	964	28	522	2,121
Total	$307	$646	$383	$2,263	$237	$944	$4,780
Total BIG	$276	$516	$8	$238	$127	$391	$1,556

(1) While the Company's exposures are shown in U.S. dollars, the obligations the Company insures are in various currencies, including U.S. dollars, Euros and British pounds sterling. Included in the table above is $133 million of reinsurance assumed on a 2004 - 2006 pool of Irish residential mortgages that is part of the Company's remaining legacy mortgage reinsurance business. One of the residential mortgage-backed securities included in the table above includes residential mortgages in both Italy and Germany, and only the portion of the transaction equal to the portion of the original mortgage pool in Italian mortgages is shown in the table.

(2) As of June 30, 2012, the Company had established a full limit loss on this exposure. The Company accelerated claims under its financial guaranty on the July payment date with respect to the 2057 bonds and intends to accelerate claims on or after the September payment date with respect to the 2037 bonds.

The Company has not guaranteed any sovereign bonds of the Selected European Countries except Greece (see Note 4, Financial Guaranty Insurance Contracts). The remainder of the "Public Finance Category" is from transactions backed by receivable payments from sub-sovereigns in Italy, Spain and Portugal. Sub-sovereign debt is debt issued by a governmental entity or government backed entity, or supported by such an entity, that is other than direct sovereign debt of the ultimate governing body of the country.

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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.

The Company monitors its investment grade credits to determine whether any new credits need to be internally downgraded to BIG. The Company 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 insured 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. The Company models most assumed RMBS credits with par above $1 million, as well as certain RMBS credits below that amount.

Credits identified as BIG are subjected to further review to determine the probability of a loss (see Note 4, Financial Guaranty Insurance Contracts). Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a lifetime loss is expected and whether a claim has been paid. The Company expects "lifetime 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 over the life of that transaction than it ultimately will have been reimbursed. For surveillance purposes, the Company calculates present value using a constant discount rate of 5%. (A risk-free rate is used for recording of reserves for financial statement purposes.)

Intense monitoring and intervention is employed for all BIG surveillance categories, with internal credit ratings reviewed quarterly. The three BIG categories are:

· BIG Category 1: Below-investment-grade transactions showing sufficient deterioration to make lifetime losses possible, but for which none are currently expected. Transactions on which claims have been paid but are expected to be fully reimbursed (other than investment grade transactions on which only liquidity claims have been paid) are in this category.

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

· BIG Category 3: Below-investment-grade transactions for which lifetime losses are expected and on which claims (other than liquidity claims) have been paid. Transactions remain in this category when claims have been paid and only a recoverable remains.

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Financial Guaranty Exposures
(Insurance and Credit Derivative Form)

	As of June 30, 2012 BIG Net Par Outstanding				Net Par Outstanding	BIG Net Par as a % of Net Par Outstanding	
	BIG 1	BIG 2	BIG 3	Total BIG			
			(in millions)				
First lien U.S. RMBS:							
Prime first lien	$76	$430	$3	$509	$690	0.1	%
Alt-A first lien	436	2,039	1,374	3,849	4,939	0.7	
Option ARM	61	471	827	1,359	1,991	0.3	
Subprime	218	1,276	864	2,358	7,754	0.4	
Second lien U.S. RMBS:							
Closed end second lien	—	450	419	869	997	0.2	
Home equity lines of credit (“HELOCs”)	394	—	2,587	2,981	3,521	0.5	
Total U.S. RMBS	1,185	4,666	6,074	11,925	19,892	2.2	
Trust preferred securities (“TruPS”)	2,071	—	952	3,023	6,006	0.5	
Other structured finance	1,261	459	1,224	2,944	78,390	0.5	
U.S. public finance	3,285	407	715	4,407	409,877	0.8	
Non-U.S. public finance (1)	2,239	276	—	2,515	38,769	0.5	
Total	$10,041	$5,808	$8,965	$24,814	$552,934	4.5	%

	As of December 31, 2011 BIG Net Par Outstanding				Net Par Outstanding	BIG Net Par as a % of Net Par Outstanding	
	BIG 1	BIG 2	BIG 3	Total BIG			
			(in millions)				
First lien U.S. RMBS:							
Prime first lien	$77	$465	$—	$542	$739	0.1	%
Alt-A first lien	1,695	1,028	1,540	4,263	5,329	0.8	
Option ARM	25	689	882	1,596	2,433	0.3	
Subprime (including net interest margin securities)	795	1,200	513	2,508	8,136	0.4	
Second lien U.S. RMBS:							
Closed end second lien	—	495	520	1,015	1,040	0.2	
HELOCs	421	—	2,858	3,279	3,890	0.6	
Total U.S. RMBS	3,013	3,877	6,313	13,203	21,567	2.4	
TruPS	2,501	—	951	3,452	6,334	0.6	
Other structured finance	1,295	548	1,429	3,272	88,028	0.6	
U.S. public finance	3,395	274	838	4,507	403,073	0.8	
Non-U.S. public finance (1)	2,046	282	—	2,328	39,046	0.4	
Total	$12,250	$4,981	$9,531	$26,762	$558,048	4.8	%

(1) Includes $276 million and $282 million in net par as of June 30, 2012 and December 31, 2011, respectively, for bonds of the Hellenic Republic of Greece, a portion of which was accelerated in July 2012 and a portion of which the

Company intends to accelerate on or after September 2012. See Note 4, Financial Guaranty Insurance Contracts.

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Below-Investment-Grade Credits
By Category

Description	As of June 30, 2012 Net Par Outstanding Financial Guaranty Insurance(1) (dollars in millions)	Credit Derivative	Total	Number of Risks(2) Financial Guaranty Insurance(1)	Credit Derivative	Total
BIG:						
Category 1	$7,467	$2,574	$10,041	164	35	199
Category 2	3,353	2,455	5,808	79	34	113
Category 3	6,894	2,071	8,965	132	25	157
Total BIG	$17,714	$7,100	$24,814	375	94	469

Description	As of December 31, 2011 Net Par Outstanding Financial Guaranty Insurance(1) (dollars in millions)	Credit Derivative	Total	Number of Risks(2) Financial Guaranty Insurance(1)	Credit Derivative	Total
BIG:						
Category 1	$8,297	$3,953	$12,250	171	40	211
Category 2	3,458	1,523	4,981	71	33	104
Category 3	7,204	2,327	9,531	126	26	152
Total BIG	$18,959	$7,803	$26,762	368	99	467

(1) Includes net par outstanding for FG 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.

4. Financial Guaranty Insurance Contracts

Change in accounting for deferred acquisition costs

In October 2010, the Financial Accounting Standards Board adopted Accounting Standards Update ("Update") No. 2010-26. This guidance was effective January 1, 2012, with retrospective application. The Update specifies that certain costs incurred in the successful acquisition of new and renewal insurance contracts should be capitalized. These costs include direct costs of contract acquisition that result directly from and are essential to the contract transaction. These costs include expenses such as ceding commissions and the cost of underwriting personnel. Management uses its judgment in determining the type and amount of cost to be deferred. The Company conducts an annual study to determine which operating costs vary with, and are directly related to, the acquisition of new business, and therefore qualify for deferral. Ceding commission income on business ceded to third party reinsurers reduces policy acquisition costs and is deferred. Costs incurred by the insurer for soliciting potential customers, market research, training, administration, unsuccessful acquisition efforts, and product development as well as all overhead type costs are charged to expense as incurred.

Expected losses, loss adjustment expenses ("LAE") and the remaining costs of servicing the insured or reinsured business are considered in determining the recoverability of deferred acquisition costs. When an insured issue is retired early, the remaining related deferred acquisition cost is expensed at that time. Ceding commission expense and income associated with future installment premiums on assumed and ceded business, respectively, are calculated at their contractually defined rates and recorded in deferred acquisition costs on the consolidated balance sheets with a corresponding offset to net premium receivable or reinsurance balances payable.

As of January 1, 2011, the effect of retrospective application of the new guidance was a reduction to deferred

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acquisition costs of $94.4 million and a reduction to retained earnings of $64.0 million.

Effect of Retrospective Application of New Deferred Acquisition Cost Guidance
On Consolidated Statements of Operations

	As Reported Second Quarter 2011	Retroactive Application Adjustment	As Revised Second Quarter 2011
	(in millions except per share amounts)		
Amortization of deferred acquisition costs	$9.5	$(3.7)	$5.8
Other operating expenses	48.5	4.7	53.2
Net income (loss)	(42.6)	(0.5)	(43.1)
Earnings per share:			
Basic	$(0.23)	$—	$(0.23)
Diluted	(0.23)	—	(0.23)

	As Reported Six Months 2011	Retroactive Application Adjustment	As Revised Six Months 2011
	(in millions except per share amounts)		
Amortization of deferred acquisition costs	$16.9	$(7.4)	$9.5
Other operating expenses	105.3	10.7	116.0
Net income (loss)	98.0	(1.8)	96.2
Earnings per share:			
Basic	0.53	(0.01)	0.52
Diluted	0.52	(0.01)	0.51

The portfolio of outstanding exposures discussed in Note 3, Outstanding Exposure, includes financial guaranty contracts that meet the definition of insurance contracts as well as those that meet the definition of derivative contracts. Amounts presented in this note relate to financial guaranty insurance contracts. Tables presented herein also present reconciliations to financial statement line items for other less significant types of insurance.

Net Earned Premiums

	Second Quarter		Six Months	
	2012	2011	2012	2011
	(in millions)			
Scheduled net earned premiums	$144.7	$202.7	$296.7	$417.6
Acceleration of premium earnings	68.2	21.0	104.8	50.6
Accretion of discount on net premiums receivable	6.3	5.8	11.0	14.8
Total financial guaranty	219.2	229.5	412.5	483.0
Other	0.1	0.5	0.5	1.0
Total net earned premiums(1)	$219.3	$230.0	$413.0	$484.0

(1) Excludes $15.5 million and $18.3 million in Second Quarter 2012 and 2011, respectively, and $32.5 million and $37.4 million for the Six Months 2012 and 2011, respectively, related to consolidated FG VIEs.

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Gross Premium Receivable, Net of Ceding Commissions Roll Forward

	Six Months	
	2012	2011
	(in millions)	
Balance beginning of period	$1,002.9	$1,167.6
Premium written, net	102.7	102.9
Premium payments received, net	(166.5)	(151.7)
Adjustments to the premium receivable:		
Changes in the expected term of financial guaranty insurance contracts	18.8	(91.1)
Accretion of discount	13.4	16.4
Foreign exchange translation	(0.5)	22.8
Consolidation of FG VIEs	(5.4)	(9.9)
Other adjustments	(1.3)	2.5
Balance, end of period (1)	$964.1	$1,059.5

(1) Excludes $31.7 million and $31.7 million as of June 30, 2012 and 2011, respectively, related to consolidated FG VIEs.

Gains or losses due to foreign exchange rate changes relate to installment premium receivables denominated in currencies other than the U.S. dollar. Approximately 49%, 47% and 51% of installment premiums at June 30, 2012, December 31, 2011 and June 30, 2011, respectively, are denominated in currencies other than the U.S. dollar, primarily in euro and British Pound Sterling.

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 Gross Premiums Receivable,
Net of Ceding Commissions (Undiscounted)

	June 30, 2012
	(in millions)
2012 (July 1 – September 30)	$48.4
2012 (October 1 – December 31)	50.0
2013	106.6
2014	93.3
2015	83.3
2016	77.3
2017-2021	305.6
2022-2026	206.6
2027-2031	152.2
After 2031	187.6
Total(1)	$1,310.9

(1) Excludes expected cash collections on FG VIEs of $37.8 million.

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Components of Unearned Premium Reserve

	As of June 30, 2012			As of December 31, 2011		
	Gross	Ceded	Net(1)	Gross	Ceded	Net(1)
	(in millions)					
Deferred premium revenue	$5,698.6	$610.6	$5,088.0	$6,046.3	$727.4	$5,318.9
Contra-paid	(123.1)	(19.8)	(103.3)	(92.2)	(18.8)	(73.4)
Total financial guaranty	5,575.5	590.8	4,984.7	5,954.1	708.6	5,245.5
Other	7.9	0.0	7.9	8.7	0.3	8.4
Total	$5,583.4	$590.8	$4,992.6	$5,962.8	$708.9	$5,253.9

(1) Total net unearned premium reserve excludes $255.5 million and $274.2 million related to FG VIEs as of June 30, 2012 and December 31, 2011, respectively.

The following table provides a schedule of the expected timing of the income statement recognition of pre-tax financial guaranty insurance net deferred premium revenue and the present value of net expected losses to be expensed. The amount and timing of actual premium earnings and loss and LAE may differ from the estimates shown below due to factors such as refundings, accelerations, commutations, changes in expected lives and updates to loss estimates. A loss and LAE reserve is only recorded for the amount by which net expected loss to be expensed exceeds deferred premium revenue determined on a contract-by-contract basis. This table excludes amounts related to consolidated FG VIEs.

Expected Timing of Premium and Loss Recognition

	As of June 30, 2012		
	Scheduled Net Earned Premium	Net Expected Loss to be Expensed	Net
	(in millions)		
2012 (July 1–September 30)	$137.9	$16.2	$121.7
2012 (October 1–December 31)	131.0	14.9	116.1
Subtotal 2012	268.9	31.1	237.8
2013	472.9	61.0	411.9
2014	434.7	48.6	386.1
2015	384.6	38.0	346.6
2016	349.1	33.7	315.4
2017 - 2021	1,325.7	142.1	1,183.6
2022 - 2026	834.5	78.5	756.0
2027 - 2031	505.6	39.5	466.1
After 2031	512.0	30.7	481.3
Total present value basis(1)(2)	5,088.0	503.2	4,584.8
Discount	279.6	275.6	4.0
Total future value	$5,367.6	$778.8	$4,588.8

(1) Balances represent discounted amounts.

(2) Consolidation of FG VIEs resulted in reductions of $381.4 million in future scheduled net earned premium and $196.8 million in net expected loss to be expensed.

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Selected Information for Policies Paid in Installments

	As of June 30, 2012	As of December 31, 2011
	(dollars in millions)	
Premiums receivable, net of ceding commission payable	$964.1	$ 1,002.9
Gross deferred premium revenue	2,013.1	2,192.6
Weighted-average risk-free rate used to discount premiums	3.6 %	3.4 %
Weighted-average period of premiums receivable (in years)	10.0	9.8

Loss Estimation Process

The Company's loss reserve committees estimate expected loss to be paid. Surveillance personnel present analyses related to potential losses to the Company's loss reserve committees for consideration in estimating the expected loss to be paid. Such analyses include the consideration of various scenarios with potential 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. In the case of its assumed business, the Company may conduct its own analysis as just described or, depending on the Company's view of the potential size of any loss and the information available to the Company, the Company may use loss estimates provided by ceding insurers. The Company's loss reserve committees review and refresh the estimate of expected loss to be paid each quarter. The Company's estimate of ultimate loss on a policy is subject to significant uncertainty over the life of the insured transaction due to the potential for significant variability in credit performance as a result of economic, fiscal and financial market variability over the long duration of most contracts. The determination of expected loss to be paid is an inherently subjective process involving numerous estimates, assumptions and judgments by management.

The following table presents a roll forward of the present value of net expected loss to be paid for financial guaranty insurance contracts by sector. Net expected loss to be paid is the estimate of the present value of future claim payments, net of reinsurance and net of salvage and subrogation, which includes the present value benefit of estimated recoveries for breaches of representations and warranties ("R&W"). The Company used weighted average risk-free rates for U.S. dollar denominated obligations, which ranged from 0.0% to 3.04% as of June 30, 2012 and 0.0% to 3.27% as of December 31, 2011.

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Present Value of Net Expected Loss to be Paid
Roll Forward by Sector(1)

	Net Expected Loss to be Paid as of March 31, 2012 (in millions)	Economic Loss Development(2)	(Paid) Recovered Losses(3)	Net Expected Loss to be Paid as of June 30, 2012(4)
U.S. RMBS:				
First lien:				
Prime first lien	$2.2	$0.7	$—	$2.9
Alt-A first lien	116.9	22.8	52.4	192.1
Option ARM	75.3	0.7	(112.3)	(36.3)
Subprime	150.4	10.6	(1.6)	159.4
Total first lien	344.8	34.8	(61.5)	318.1
Second lien:				
Closed-end second lien	(89.7)	(2.6)	75.9	(16.4)
HELOCs	(42.5)	14.8	(36.0)	(63.7)
Total second lien	(132.2)	12.2	39.9	(80.1)
Total U.S. RMBS	212.6	47.0	(21.6)	238.0
TruPS	8.5	(1.8)	(0.2)	6.5
Other structured finance	196.8	30.9	(6.6)	221.1
U.S. public finance	32.7	35.5	(9.8)	58.4
Non-U.S. public finance	301.8	(15.0)	15.7	302.5
Total financial guaranty	752.4	96.6	(22.5)	826.5
Other	1.9	(6.0)	—	(4.1)
Total	$754.3	$90.6	$(22.5)	$822.4

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	Net Expected Loss to be Paid as of March 31, 2011 (in millions)	Economic Loss Development(2)	(Paid) Recovered Losses(3)	Net Expected Loss to be Paid as of June 30, 2011
U.S. RMBS:				
First lien:				
Prime first lien	$1.5	$1.7	$—	$3.2
Alt-A first lien	171.4	15.3	(19.1)	167.6
Option ARM	322.1	26.3	(81.5)	266.9
Subprime	167.5	(5.4)	(0.6)	161.5
Total first lien	662.5	37.9	(101.2)	599.2
Second lien:				
Closed-end second lien	(76.9)	(3.2)	(14.6)	(94.7)
HELOCs	(792.7)	27.1	727.3	(38.3)
Total second lien	(869.6)	23.9	712.7	(133.0)
Total U.S. RMBS	(207.1)	61.8	611.5	466.2
TruPS	(0.9)	7.0	(1.4)	4.7
Other structured finance	173.9	1.2	0.8	175.9
U.S. public finance	55.9	3.7	(0.2)	59.4
Non-U.S. public finance	10.4	(3.6)	—	6.8
Total financial guaranty	32.2	70.1	610.7	713.0
Other	2.1	—	—	2.1
Total	$34.3	$70.1	$610.7	$715.1

	Net Expected Loss to be Paid as of December 31, 2011(4) (in millions)	Economic Loss Development(2)	(Paid) Recovered Losses(3)	Net Expected Loss to be Paid as of June 30, 2012(4)
U.S. RMBS:				
First lien:				
Prime first lien	$1.8	$1.1	$—	$2.9
Alt-A first lien	134.9	14.2	43.0	192.1
Option ARM	152.9	(1.0)	(188.2)	(36.3)
Subprime	140.3	21.9	(2.8)	159.4
Total first lien	429.9	36.2	(148.0)	318.1
Second lien:				
Closed-end second lien	(79.6)	(3.7)	66.9	(16.4)
HELOCs	(31.1)	22.4	(55.0)	(63.7)
Total second lien	(110.7)	18.7	11.9	(80.1)
Total U.S. RMBS	319.2	54.9	(136.1)	238.0
TruPS	13.2	(6.3)	(0.4)	6.5
Other structured finance	239.6	11.6	(30.1)	221.1
U.S. public finance	15.8	58.3	(15.7)	58.4
Non-U.S public finance	50.2	182.9	69.4	302.5
Total financial guaranty	638.0	301.4	(112.9)	826.5
Other	1.9	(6.0)	—	(4.1)

Total	$639.9	$295.4	$(112.9)	$822.4

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	Net Expected Loss to be Paid as of December 31, 2010 (in millions)	Economic Loss Development(2)	(Paid) Recovered Losses(3)	Expected Loss to be Paid as of June 30, 2011
U.S. RMBS:				
First lien:				
Prime first lien	$1.4	$1.8	$—	$3.2
Alt-A first lien	184.4	21.8	(38.6)	167.6
Option ARM	523.7	(88.4)	(168.4)	266.9
Subprime	200.4	(23.2)	(15.7)	161.5
Total first lien	909.9	(88.0)	(222.7)	599.2
Second lien:				
Closed-end second lien	56.6	(109.6)	(41.7)	(94.7)
HELOCs	(805.7)	104.7	662.7	(38.3)
Total second lien	(749.1)	(4.9)	621.0	(133.0)
Total U.S. RMBS	160.8	(92.9)	398.3	466.2
TruPS	(0.6)	7.0	(1.7)	4.7
Other structured finance	159.7	17.5	(1.3)	175.9
U.S. public finance	81.6	(13.0)	(9.2)	59.4
Non-U.S public finance	7.3	(0.5)	—	6.8
Total financial guaranty	408.8	(81.9)	386.1	713.0
Other	2.1	—	—	2.1
Total	$410.9	$(81.9)	$386.1	$715.1

(1) Amounts include all expected payments whether or not the insured VIE is consolidated.

(2) 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.

(3) 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.

(4) Includes expected LAE to be paid for mitigating claim liabilities of $31.1 million as of June 30, 2012 and $35.5 million as of December 31, 2011.

The table below provides a reconciliation of expected loss to be paid to 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 payments that have been made but have not yet been expensed, (2) for transactions with a net expected recovery, the addition of claim payments that have been made (and therefore are not included in expected loss to be paid) that are expected to be recovered in the future (and therefore have also reduced expected loss to be paid), and (3) loss reserves that have already been established (and therefore expensed but not yet paid).

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

	As of June 30, 2012 (in millions)
Net expected loss to be paid	$826.5
Less: net expected loss to be paid for FG VIEs	(65.7)
Total	892.2
Contra-paid, net	103.3
Salvage and subrogation recoverable	370.8
Ceded salvage and subrogation recoverable(1)	(40.3)
Loss and LAE reserve	(992.0)
Reinsurance recoverable on unpaid losses	169.2
Net expected loss to be expensed(2)	$503.2

(1) Recorded in reinsurance balances payable on the consolidated balance sheet.

(2) Excludes $196.8 million related to consolidated FG VIEs.

The Company’s 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 to the projected performance of the collateral over time. The resulting projected claim payments or reimbursements are then discounted using risk-free rates. For transactions where the Company projects it will receive recoveries from providers of R&W, it projects the amount of recoveries and either establishes a recovery for claims already paid or reduces its projected claim payments accordingly.

The further behind a mortgage borrower falls in making payments, the more likely it is that he or she will default. The rate at which borrowers from a particular delinquency category (number of monthly payments behind) eventually default is referred to as the “liquidation rate.” Liquidation rates may be derived from observed roll rates, which are the rates at which loans progress from one delinquency category to the next and eventually to default and liquidation. The Company applies liquidation rates to the mortgage loan collateral in each delinquency category and makes certain timing assumptions to project near-term mortgage collateral defaults from loans that are currently delinquent.

Mortgage borrowers that are not more than one payment behind (generally considered performing borrowers) have demonstrated an ability and willingness to pay throughout the recession and mortgage crisis, and as a result are viewed as less likely to default than delinquent borrowers. Performing borrowers that eventually default will also need to progress through delinquency categories before any defaults occur. The Company projects how many of the currently performing loans will default and when they will default, by first converting the projected near term defaults of delinquent borrowers derived from liquidation rates into a vector of conditional default rates "CDR", then projecting how the conditional default rates will develop over time. Loans that are defaulted pursuant to the conditional default rate after the liquidation of currently delinquent loans represent defaults of currently performing loans. A conditional default rate is the outstanding principal amount of defaulted loans liquidated in the current month divided by the remaining outstanding amount of the whole pool of loans (or “collateral pool balance”). The collateral pool balance decreases over time as a result of scheduled principal payments, partial and whole principal prepayments, and defaults.

In order to derive collateral pool losses from the collateral pool defaults it has projected, the Company applies a loss severity. The loss severity is the amount of loss the transaction experiences on a defaulted loan after the application of net proceeds from the disposal of the underlying property. The Company projects loss severities by sector based on its experience to date. Further detail regarding the assumptions and variables the Company used to project collateral losses in its U.S. RMBS portfolio may be found below in the sections "U.S. Second Lien RMBS Loss Projections: HELOCs and Closed-End Second Lien" and "U.S. First Lien RMBS Loss Projections: Alt-A First Lien, Option ARM, Subprime and Prime."

The Company is in the process of enforcing claims for breaches of R&W regarding the characteristics of the loans

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included in the collateral pools. The Company calculates a credit from the RMBS issuer for such recoveries where the R&W were provided by an entity the Company believes to be financially viable and where the Company already has access or
believes it will attain access to the underlying mortgage loan files. Where the Company has an agreement with an R&W provider (e.g., the the Bank of America Agreement or the Deutsche Bank Agreement) or where it is in advanced discussions on a potential agreement, that credit is based on the agreement or potential agreement. In second lien RMBS transactions where there is no agreement or advanced discussions, this credit is based on a percentage of actual repurchase rates achieved across those transactions where material repurchases have been made. In first lien RMBS transactions where there is no agreement or advanced discussions, this credit is estimated by reducing collateral losses projected by the Company to reflect a percentage of the recoveries the Company believes it will achieve, based on a percentage of actual repurchase rates achieved or based on the amounts the Company was able to negotiate under the Bank of America Agreement and Deutsche Bank Agreement. The first lien approach is different from the second lien approach because the Company's first lien transactions have multiple tranches and a more complicated method is required to correctly allocate credit to each tranche. In each case, the credit is a function of the projected lifetime collateral losses in the collateral pool, so an increase in projected collateral losses generally increases the R&W credit calculated by the Company for the RMBS issuer. Further detail regarding how the Company calculates these credits may be found under "Breaches of Representations and Warranties" below.

The Company projects the overall future cash flow from a collateral pool by adjusting the payment stream from the principal and interest contractually due on the underlying mortgages for (a) the collateral losses it projects as described above, (b) assumed voluntary prepayments and (c) recoveries for breaches of R&W as described above. The Company then applies an individual model of the structure of the transaction to the projected future cash flow from that transaction's collateral pool to project the Company's future claims and claim reimbursements for that individual transaction. Finally, the projected claims and reimbursements are discounted using risk-free rates. As noted above, the Company runs several sets of assumptions regarding mortgage collateral performance, or scenarios, and probability weights them.

Second Quarter-End 2012 U.S. RMBS Loss Projections

The Company retained the same general approach and methodology to projecting RMBS performance at June 30, 2012 as it did at March 31, 2012 and December 31, 2011. The approach combines using each transaction's observed data with the Company's estimate of how the transaction will ultimately perform based on the Company's view of the magnitude and timing of a recovery in the mortgage market. During the quarter the Company observed both positive and negative developments in the market. These developments were reflected by moderately lowering the initial CDR's which are a function of the observed delinquency data, and by adjusting the scenarios used to project the amount of time until the RMBS market stabilizes.

The scenarios the Company used to project first and second lien RMBS collateral losses at June 30, 2012 were essentially the same as those it used at March 31, 2012 and December 31, 2011, except that (i) based on its observation of the continued elevated levels of early stage delinquencies, the Company updated its projections to reflect a slower recovery in its base cases and (ii) the Company reduced the time until the market stabilizes in its most optimistic case by three months, so it assumed that the recovery projected last quarter was occurring at the expected pace and (iii) the Company adjusted its most pessimistic case, where it assumed the recovery would happen six months more slowly than what was assumed last quarter.

The Company also used generally the same methodology and assumptions to project the credit received for recoveries in R&W at June 30, 2012 as March 31, 2012 and December 31, 2011. The primary differences relate to a change in assumption regarding the likelihood and amount of recovery from certain R&W providers.

U.S. Second Lien RMBS Loss Projections: HELOCs and Closed-End Second Lien

The Company insures two types of second lien RMBS: those secured by HELOCs and those secured by closed end second lien mortgages. HELOCs are revolving lines of credit generally secured by a second lien on a one to four family home. A mortgage for a fixed amount secured by a second lien on a one to four family home is generally referred to as a closed end second lien. Second lien RMBS sometimes include a portion of loan collateral with a different priority than the majority of the collateral. The Company has material exposure to second lien mortgage loans originated and serviced by a number of parties, but the Company's most significant second lien exposure is to HELOCs originated and serviced by Countrywide, a subsidiary of Bank of America. See "—Breaches of Representations and Warranties."

The delinquency performance of HELOC and closed end second lien exposures included in transactions insured by the Company began to deteriorate in 2007, and such transactions, continue to perform below the Company's original underwriting expectations. While insured securities benefit from structural protections within the transactions designed to absorb collateral losses in excess of previous historically high levels, in many second lien RMBS projected losses now exceed

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those structural protections.

The Company believes the primary variables affecting its expected losses in second lien RMBS transactions are the amount and timing of future losses in the collateral pool supporting the transactions and the amount of loans repurchased for breaches of R&W (or agreements with R&W providers related to such obligations). Expected losses are also a function of the structure of the transaction; the voluntary prepayment rate (typically also referred to as conditional prepayment rate "CPR" of the collateral); the interest rate environment; and assumptions about the draw rate and loss severity. These variables are interrelated, difficult to predict and subject to considerable volatility. If actual experience differs from the Company's assumptions, the losses incurred could be materially different from the estimate. The Company continues to update its evaluation of these exposures as new information becomes available.

The following table shows the key assumptions used in the calculation of estimated expected loss to be paid for direct vintage 2004 - 2008 second lien U.S. RMBS.

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

HELOC key assumptions	As of June 30, 2012	As of March 31, 2012	As of December 31, 2011
Plateau CDR	2.9% – 20.9%	3.3% – 26.3%	4.0% – 27.4%
Final CDR trended down to	0.4% – 3.2%	0.4% – 3.2%	0.4% – 3.2%
Expected period until final CDR	36 months	36 months	36 months
Initial CPR	2.7% – 16.4%	2.6% – 15.1%	1.4% – 25.8%
Final CPR	10%	10%	10%
Loss severity	98%	98%	98%
Initial draw rate	0.0% – 4.1%	0.0% – 7.8%	0.0% – 15.3%

Closed-end second lien key assumptions	As of June 30, 2012	As of March 31, 2012	As of December 31, 2011
Plateau CDR	4.3% – 20.7%	5.4% – 24.9%	6.9% – 24.8%
Final CDR trended down to	3.3% – 9.1%	3.3% – 9.2%	3.5% – 9.2%
Expected period until final CDR	36 months	36 months	36 months
Initial CPR	1.1% – 11.0%	1.2% – 8.6%	0.9% – 14.7%
Final CPR	10%	10%	10%
Loss severity	98%	98%	98%

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

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 (the percent of loans in a given delinquency status that are assumed to ultimately default) from selected representative transactions and then applying an average of the preceding twelve months' liquidation rates to the amount of loans in the delinquency categories. The amount of loans projected to default in the first through fifth months is expressed as a CDR. The first four months' CDR is calculated by applying the liquidation rates to the current period past due balances (i.e., the 150-179 day balance is liquidated in the first projected month, the 120-149 day balance is liquidated in the second projected month, the

90-119 day balance is liquidated in the third projected month and the 60-89 day balance is liquidated in the fourth projected month). For the fifth month the CDR is calculated using the average 30-59 day past due balances for the prior three months. An average of the third, fourth and fifth month CDR is then used as the basis for the plateau period that follows the embedded five months of losses.

As of June 30, 2012, for the base case scenario, the CDR (the “plateau CDR”) was held constant for one month.

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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. In the base case scenario, the time over which the CDR trends down to its final CDR is 30 months. Therefore, the total stress period for second lien transactions is 36 months, comprising five months of delinquent data, a one month plateau period and 30 months of decrease to the steady state CDR. This is the same as March 31, 2012 and December 31, 2011. The long-term steady state CDR are calculated as the constant CDR that would have yielded the amount of losses originally expected at underwriting. When a second lien loan defaults, there is generally a very low recovery. Based on current expectations of future performance, the Company assumes that it will only recover 2% of the collateral, the same as March 31, 2012 and December 31, 2011.

The rate at which the principal amount of loans is prepaid may impact both the amount of losses projected (which is a function of the CDR and the loan balance over time) as well as the amount of excess spread (which is the excess of the interest paid by the borrowers on the underlying loan over the amount of interest and expenses owed on the insured obligations). In the base case, the current CPR is assumed to continue until the end of the plateau before gradually increasing to the final CPR over the same period the CDR decreases. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant. The final CPR is assumed to be 10% for both HELOC and closed-end second lien transactions. This level is much higher than current rates for most transactions, but lower than the historical average, which reflects the Company’s continued uncertainty about the projected performance of the borrowers in these transactions. This pattern is consistent with how the Company modeled the CPR at March 31, 2012 and December 31, 2011. 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, and HELOC draw rates (the amount of new advances provided on existing HELOCs expressed as a percentage of current outstanding advances). For HELOC transactions, the draw rate is assumed to decline from the current level to a final draw rate over a period of three months. The final draw rates were assumed to range from 0.0% to 2.1%.

In estimating expected losses, the Company modeled and probability weighted three possible CDR curves applicable to the period preceding the return to the long-term steady state CDR. The Company believes that the level of the elevated CDR and the length of time it will persist is the primary driver behind the likely amount of losses the collateral will suffer (before considering the effects of repurchases of ineligible loans). The Company continues to evaluate the assumptions affecting its modeling results.

At June 30, 2012, the Company’s base case assumed a one month CDR plateau and a 30 month ramp-down (for a total stress period of 36 months), the same as March 31, 2012 and December 31, 2011. The Company also modeled a scenario with a longer period of elevated defaults and another with a shorter period of elevated defaults and weighted them the same as of March 31, 2012 and December 31, 2011, but in each case changed the length of the ramp-downs by three months (and so the length of elevated defaults) in order to reflect both positive and negative developments observed by the Company in the market. Increasing the CDR plateau to four months and increasing the ramp-down by three months to 33-months (rather than 30 months at March 31, 2012 and December 31, 2011, for a total stress period of 42 months rather than 39 months as at March 31, 2012 and December 31, 2011) would increase the expected loss by approximately $64.9 million for HELOC transactions and $3.9 million for closed-end second lien transactions. On the other hand, keeping the CDR plateau at one month but decreasing the length of the CDR ramp-down to a 21 months (rather than 24 months as at March 31, 2012 and December 31, 2011, for a total stress period of 33 months rather than 30 months as at March 31, 2012 and December 31, 2011) would decrease the expected loss by approximately $65.3 million for HELOC transactions and $2.9 million for closed-end second lien transactions.

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

First lien RMBS are generally categorized in accordance with the characteristics of the first lien mortgage loans on one-to-four family homes supporting the transactions. The collateral supporting “subprime RMBS” transactions consists of first-lien residential mortgage loans made to subprime borrowers. A “subprime borrower” is one considered to be a higher risk credit based on credit scores or other risk characteristics. Another type of RMBS transaction is generally referred to as “Alt-A first lien.” The collateral supporting such transactions consists of first-lien residential mortgage loans made to “prime” quality borrowers who lack certain ancillary characteristics that would make them prime. When more than 66% of the loans originally included in the pool are mortgage loans with an option to make a minimum payment that has the potential to amortize the loan negatively (i.e., increase the amount of principal owed), the transaction is referred to as an “Option ARM.” Finally, transactions may be composed primarily of loans made to prime borrowers. First lien RMBS sometimes include a portion of loan collateral that differs in priority from the majority of the collateral.

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The performance of the Company's first lien RMBS exposures began to deteriorate in 2007 and such transactions, continue to perform below the Company's original underwriting expectations. The Company currently projects first lien collateral losses many times those expected at the time of underwriting. While insured securities benefited from structural protections within the transactions designed to absorb some of the collateral losses, in many first lien RMBS transactions, projected losses exceed those structural protections.

The majority of projected losses in first lien RMBS transactions are expected to come from non-performing mortgage loans (those that are delinquent or in foreclosure or where the loan has been foreclosed and the RMBS issuer owns the underlying real estate). Changes in the amount of non-performing loans from the amount projected in the previous period is 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 delinquency categories. The Company arrived at its liquidation rates based on data purchased from a third party, and assumptions about how delays in the foreclosure process may ultimately affect the rate at which loans are liquidated. The liquidation rate is a standard industry measure that is used to estimate the number of loans in a given aging category that will default within a specified time period. The Company projects these liquidations to occur over two years. The Company used the same liquidation rates for June 30, 2012 as it did for March 31, 2012 and December 31, 2011. The following table shows liquidation assumptions for various delinquency categories.

First Lien Liquidation Rates
as of June 30, 2012

30 – 59 Days Delinquent	
Alt A and Prime	35%
Option ARM	50
Subprime	30
60 – 89 Days Delinquent	
Alt A and Prime	55
Option ARM	65
Subprime	45
90+ Days Delinquent	
Alt A and Prime	65
Option ARM	75
Subprime	60
Bankruptcy	
Alt A and Prime	55
Option ARM	70
Subprime	50
Foreclosure	
Alt A and Prime	85
Option ARM	85
Subprime	80
Real Estate Owned ("REO")	
All	100

While the Company uses liquidation rates as described above to project defaults of non-performing loans, it projects defaults on presently current loans by applying a CDR trend. The start of that CDR trend is based on the defaults the Company projects will emerge from currently nonperforming 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 24 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, 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. Under the Company's methodology, defaults projected to occur in the first 24 months represent

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defaults that can be attributed to loans that are currently delinquent or in foreclosure, while the defaults projected to occur using the projected CDR trend after the first 24 month period represent defaults attributable to borrowers that are currently performing.

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 historic high levels, and the Company is assuming that these high levels generally will continue for another year (in the case of subprime loans, the Company assumes the unprecedented 90% loss severity rate will continue for six months then drop to 80% for six months before following the ramp described below). The Company determines its initial loss severity based on actual recent experience. The Company's loss severity assumptions for June 30, 2012 were the same as it used for March 31, 2012 and December 31, 2011. The Company then assumes that loss severities begin returning to levels consistent with underwriting assumptions beginning in June 2013, and in the base case scenario, decline over two years to 40%.

The following table shows the key assumptions used in the calculation of expected loss to be paid for direct vintage 2004 - 2008 first lien U.S. RMBS.

Key Assumptions in Base Case Expected Loss Estimates
First Lien RMBS

	As of June 30, 2012		As of March 31, 2012		As of December 31, 2011	
Alt-A First Lien						
Plateau CDR	3.3	%– 23.0%	2.7	%– 33.9%	2.8	%– 41.3%
Intermediate CDR	0.7	%– 4.6%	0.5	%– 6.8%	0.6	%– 8.3%
Final CDR	0.2	%– 1.2%	0.1	%– 1.7%	0.1	%– 2.1%
Initial loss severity	65%		65%		65%	
Initial CPR	0.0	%– 27.1%	0.0	%– 34.1%	0.0	%– 24.4%
Final CPR	15%		15%		15%	
Option ARM						
Plateau CDR	9.3	%– 30.2%	9.7	%– 32.2%	11.7	%– 31.5%
Intermediate CDR	1.9	%– 6.0%	1.9	%– 6.4%	2.3	%– 6.3%
Final CDR	0.5	%– 1.5%	0.5	%– 1.6%	0.6	%– 1.6%
Initial loss severity	65%		65%		65%	
Initial CPR	0.6	%– 4.9%	0.1	%– 5.3%	0.3	%– 10.8%
Final CPR	15%		15%		15%	
Subprime						
Plateau conditional default rate	7.2	%– 29.2%	8.3	%– 30.0%	8.6	%– 29.9%
Intermediate conditional default rate	1.4	%– 5.8%	1.7	%– 6.0%	1.7	%– 6.0%
Final conditional default rate	0.4	%– 1.5%	0.4	%– 1.5%	0.4	%– 1.5%
Initial loss severity	90%		90%		90%	
Initial CPR	0.0	%– 8.8%	0.0	%– 8.8%	0.0	%– 16.3%
Final CPR	15%		15%		15%	

The rate at which the principal amount of loans is prepaid may impact both the amount of losses projected (since that amount is a function of the conditional default rate, 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 CPR follows a similar pattern to that of the conditional default rate. 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 either 10% or 15% depending on the scenario run. For transactions where the initial CPR is higher than the final CPR, the initial CPR is held constant.

The ultimate performance of the Company's first lien RMBS transactions remains highly uncertain and may be

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subject to considerable volatility due to the influence of many factors, including the level and timing of loan defaults, changes in housing prices and other variables. The Company will continue to monitor the performance of its RMBS exposures and will adjust the loss projections for those transactions based on actual performance and management's estimates of future performance.

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 conditional default rate returned to its modeled equilibrium, which was defined as 5% of the current conditional default rate. The Company also stressed CPR and the speed of recovery of loss severity rates. The Company probability weighted a total of five scenarios (including its base case) at June 30, 2012, the same number of scenarios as March 31, 2012 and December 31, 2011. For June 30, 2012 the Company assumed in the most stressful scenario that the recovery would occur three months more slowly and in the most optimistic scenario that it would occur three months more quickly than it had for March 31, 2012 and December 31, 2011, but otherwise used the same scenarios and weightings for June 30, 2012 as March 31, 2012 and December 31, 2011. In a somewhat more stressful environment than that of the base case, where the conditional default rate plateau was extended three months (to be 27 months long) before the same more gradual conditional default rate recovery and loss severities were assumed to recover over four rather than two years (and subprime loss severities were assumed to recover only to 60%), expected loss to be paid would increase from current projections by approximately $26.9 million for Alt-A first liens, $25.6 million for Option ARM, $112.2 million for subprime and $1.2 million for prime transactions. In an even more stressful scenario where loss severities were assumed to rise and then recover over eight years and the initial ramp-down of the conditional default rate was assumed to occur over 15 months (rather than 12 months as at March 31, 2012 and December 31, 2011) and other assumptions were the same as the other stress scenario, expected loss to be paid would increase from current projections by approximately $75.4 million for Alt-A first liens, $63.3 million for Option ARM, $174.5 million for subprime and $3.5 million for prime transactions. The Company also considered two scenarios where the recovery was faster than in its base case. In a scenario with a somewhat less stressful environment than the base case, where conditional default rate recovery was somewhat less gradual and the initial subprime loss severity rate was assumed to be 80% for 12 months and was assumed to recover to 40% over two years, expected loss to be paid would decrease from current projections by approximately $5.1 million for Alt-A first lien, $30.3 million for Option ARM, $26.8 million for subprime and $0.1 million for prime transactions. In an even less stressful scenario where the conditional default rate plateau was three months shorter (21 months, effectively assuming that liquidation rates would improve) and the conditional default rate recovery was more pronounced, (including an initial ramp-down of the conditional default rate over nine months rather than 12 months as at March 31, 2012 and December 31, 2011), expected loss to be paid would decrease from current projections by approximately $31.1 million for Alt-A first lien, $73.7 million for Option ARM, $54.0 million for subprime and $0.9 million for prime transactions.

Breaches of Representations and Warranties

The Company is pursuing reimbursements for breaches of R&W regarding loan characteristics. Performance of the collateral underlying certain first and second lien securitizations has substantially differed from the Company's original expectations. The Company has employed several loan file diligence firms and law firms as well as devoted internal resources to review the mortgage files surrounding many of the defaulted loans. The Company's success in these efforts has resulted in three negotiated agreements in respect of the Company's R&W claims, including one on April 14, 2011 with Bank of America and one on May 8, 2012 with Deutsche Bank AG as described under "Deutsche Bank Agreement" in Note 2, Business Changes, Uncertainties and Accounting Developments.

The Company has included in its net expected loss estimates as of June 30, 2012 an estimated benefit from loan repurchases related to breaches of R&W of $1.2 billion, which includes $546.7 million from Bank of America and Deutsche Bank AG under their respective agreements and $666.2 million in transactions where the Company does not

yet have such an agreement. Proceeds projected to be reimbursed to the Company on transactions where the Company has already paid claims are viewed as a recovery on paid losses. For transactions where the Company has not already paid claims, projected recoveries reduce projected loss estimates. In either case, projected recoveries have no effect on the amount of the Company's exposure. These amounts reflect payments made pursuant to the negotiated transaction agreements and not payments made pursuant to legal settlements. See “-Recovery Litigation” below for a description of the related legal proceedings the Company has commenced.

The Company's success in pursuing breaches of R&W is based upon a detailed review of loan files. The company reviewed approximately 34,200 second lien and 6,800 first lien loan files (representing approximately $2,593 million and $2,357 million, respectively, of loans) in financial guaranty transactions as to which it eventually reached agreements, including the agreements with Bank of America and Deutsche Bank. For the RMBS transactions as to which the Company had not settled its claims for breaches of R&W as of June 30, 2012, the Company had performed a detailed review of

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approximately 11,000 second lien and 20,300 first lien loan files, representing approximately $812 million in second lien and $6,293 million in first lien outstanding par of loans underlying insured transactions. In the majority of its loan file reviews, the Company identified breaches of one or more R&W regarding the characteristics of the loans, such as misrepresentation of income or employment of the borrower, occupancy, undisclosed debt and non-compliance with underwriting guidelines at loan origination.

Through June 30, 2012 the Company has caused entities providing R&Ws to pay or agree to pay approximately $2.6 billion in respect of their R&W liabilities for transactions in which the Company has provided a financial guaranty. Of this, $2.0 billion are payments made or to be made directly to the Company pursuant to agreements with R&W providers (e.g. the Bank of America Agreement and Deutsche Bank Agreement) and approximately $602 million are amounts paid (or committed to be paid) into the relevant RMBS financial guaranty transactions pursuant to the transaction documents.

The $2.0 billion of payments made or to be made directly to the Company by R&W providers under agreements with the Company includes $1,473 million that has already been received by the Company, as well as $568 million (gross of reinsurance) the Company projects receiving in the future pursuant to such currently existing agreements. Because most of that $568 million is projected to be received through loss-sharing arrangements, the exact amount the Company will receive will depend on actual losses experienced by the covered transactions. This amount is included in the Company's calculated credit for R&W recoveries, described below.

The $602 million paid, or committed to be paid, by R&W providers into the relevant RMBS transactions pursuant to the transaction documents flow through the transaction “waterfalls.” Because the Company may insure only a portion of the capital structure of a transaction, such payments will not necessarily directly benefit the Company dollar-for-dollar, especially in first lien transactions. However, such payments do reduce collateral pool losses and so usually reduce the Company's expected losses.

The Company did not incorporate any gain contingencies or damages paid from potential litigation in its estimated repurchases. The amount the Company will ultimately recover related to contractual R&W is uncertain and subject to a number of factors including the counterparty’s ability to pay, the number and loss amount of loans determined to have breached R&W and, potentially, negotiated settlements or litigation recoveries. As such, the Company’s estimate of recoveries is uncertain and actual amounts realized may differ significantly from these estimates. In arriving at the expected recovery from breaches of R&W, the Company considered the creditworthiness of the provider of the R&W, the number of breaches found on defaulted loans, the success rate in resolving these breaches across those transactions where material repurchases have been made and the potential amount of time until the recovery is realized.

The calculation of expected recovery from breaches of R&W involved a variety of scenarios which ranged from the Company recovering substantially all of the losses it incurred due to violations of R&W to the Company realizing limited recoveries. The Company did not include any recoveries related to breaches of R&W in amounts greater than the losses it paid or expected to pay under any given cash flow scenario. These scenarios were probability weighted in order to determine the recovery incorporated into the Company’s estimate of expected losses. This approach was used for both loans that had already defaulted and those assumed to default in the future.

Balance Sheet Classification of R&W Benefit, Net of Reinsurance

	As of June 30, 2012			As of December 31, 2011		
	For all Financial Guaranty Insurance	Effect of Consolidating FG VIEs	Reported on Balance Sheet(1)	For all Financial Guaranty Insurance	Effect of Consolidating FG VIEs	Reported on Balance Sheet(1)

	Contracts (in millions)			Contracts		
Salvage and subrogation recoverable	$313.1	$(124.5)	$ 188.6	$401.8	$(197.3)	$ 204.5
Loss and LAE reserve	740.7	(39.8)	700.9	857.5	(74.6)	782.9

(1) The remaining benefit for R&W is not recorded on the balance sheet until the expected loss, net of R&W, exceeds unearned premium reserve.

The following table represents the Company's total estimated R&W recoveries netted in expected loss to be paid, from defective mortgage loans included in certain first and second lien U.S. RMBS loan securitizations that it insures.

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Roll Forward of Estimated Benefit from
Recoveries from Representation and Warranty Breaches, Net of Reinsurance

	Future Net R&W Benefit as of December 31, 2011	R&W Development and Accretion of Discount During Six Months 2012	R&W Recovered During Six Months 2012(1)	Future Net R&W Benefit as of June 30, 2012
	(in millions)			
Prime first lien	$3.0	$ 1.0	$—	$ 4.0
Alt-A first lien	202.7	21.0	(64.2)	159.5
Option ARM	713.9	59.0	(75.8)	697.1
Subprime	101.5	(8.1)	(0.1)	93.3
Closed end second lien	223.8	(2.0)	(84.9)	136.9
HELOC	189.9	(0.2)	(67.6)	122.1
Total	$1,434.8	$ 70.7	$(292.6)	$ 1,212.9

	Future Net R&W Benefit as of December 31, 2010	R&W Development and Accretion of Discount During Six Months 2011	R&W Recovered During Six Months 2011(1)	Future Net R&W Benefit as of June 30, 2011
	(in millions)			
Prime first lien	$1.1	$ 1.8	$—	$ 2.9
Alt-A first lien	81.0	46.6	—	127.6
Option ARM	309.3	449.2	(47.3)	711.2
Subprime	26.8	54.7	—	81.5
Closed end second lien	178.2	61.5	—	239.7
HELOC	1,004.1	157.1	(850.8)	310.4
Total	$1,600.5	$ 770.9	$(898.1)	$ 1,473.3

(1) Gross amounts recovered were $311.4 million and $1,015.0 million in Six Months 2012 and 2011, respectively.

Financial Guaranty Insurance U.S. RMBS Risks with R&W Benefit

	Number of Risks (1) as of		Debt Service as of	
	June 30, 2012	December 31, 2011	June 30, 2012	December 31, 2011
	(dollars in millions)			
Prime first lien	1	1	$39.3	$41.9
Alt-A first lien	19	22	1,492.9	1,732.6
Option ARM	10	12	1,129.4	1,459.7
Subprime	5	5	842.0	905.8
Closed-end second lien	4	4	245.3	361.4
HELOC (2)	6	15	543.6	2,978.5

Total	45	59	$4,292.5	$7,479.9

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

(2) The decline in number of HELOC risks and debt service relates to the final payment from Bank of America for covered HELOC transactions.

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The following table provides a breakdown of the development and accretion amount in the roll forward of estimated recoveries associated with alleged breaches of R&W.

	Second Quarter		Six Months	
	2012	2011	2012	2011
	(in millions)			
Inclusion or removal of deals with breaches of R&W during period	$(5.0)	$—	$(5.0)	$107.1
Change in recovery assumptions as the result of additional file review and recovery success	(10.0)	—	69.7	198.4
Estimated increase (decrease) in defaults that will result in additional (lower) breaches	50.9	(5.8)	(0.4)	34.0
Results of settlements	—	95.6	—	429.7
Accretion of discount on balance	2.4	1.1	6.4	1.7
Total	$38.3	$90.9	$70.7	$770.9

The R&W development during Second Quarter 2012 resulted primarily from the change in projected future defaults offset by an adjustment to the projected recovery from one counterparty. The Company also eliminated the credit in two instances where the Company has become less confident that it will obtain the loan files.

The Company assumes that recoveries on transactions backed by HELOC and closed-end second lien loans that were not subject to the Bank of America Agreement or Deutsche Bank Agreement will occur in two to four years from the balance sheet date depending on the scenarios, and that recoveries on transactions backed by Alt-A first lien, Option ARM and Subprime loans will occur as claims are paid over the life of the transactions. Recoveries on second lien transactions subject to the Bank of America Agreement were paid in full by March 31, 2012.

As of June 30, 2012, cumulative collateral losses on the first lien RMBS transactions subject to a comprehensive agreement with Bank of America Corporation and its subsidiaries, including Countrywide Financial Corporation and its subsidiaries (collectively, “Bank of America”), 20 of which were transactions as to which the Company issued financial guaranty insurance contracts and one of which was a transaction on which the Company sold protection through a CDS (the “Bank of America Agreement”), were approximately $2.5 billion and $0.09 billion, respectively. The Company estimates that cumulative projected collateral losses for the 20 financial guaranty insurance transactions and one CDS transaction will be $5.0 billion and $0.2 billion, respectively. The Bank of America Agreement covers cumulative collateral losses up to $6.6 billion for all these transactions. Bank of America had placed approximately $1.0 billion of eligible assets in trust in order to collateralize the reimbursement obligation relating to these and one covered first lien CDS transaction. The amount of assets required to be posted may increase or decrease from time to time as determined by rating agency requirements.

On May 8, 2012, Assured Guaranty reached a settlement with Deutsche Bank AG and certain of its affiliates (collectively, “Deutsche Bank”), resolving claims related to certain RMBS transactions issued, underwritten or sponsored by Deutsche Bank that were insured by Assured Guaranty under financial guaranty insurance policies and to certain RMBS exposures in re-securitization transactions as to which Assured Guaranty provides credit protection through CDS. See Note 2, Business Changes, Risks, Uncertainties and Accounting Developments for more information.

Student Loan Transactions

The Company has insured or reinsured $2.7 billion net par of student loan securitizations, of which $1.4 billion was issued by private issuers and classified as asset-backed and $1.3 billion was issued by public authorities and classified

as public finance. Of these amounts, $170.1 million and $447.4 million, respectively, are rated BIG. The Company is projecting approximately $62.7 million of net expected loss to be paid in these portfolios. In general, the losses are due to: (i) the poor credit performance of private student loan collateral and high loss severities; (ii) high interest rates on auction rate securities with respect to which the auctions have failed or (iii) lower risk-free rates used for discounting, which result in higher present value losses on transactions where losses are payable at final maturity. The largest of these losses was approximately $27.4 million and related to a transaction backed by a pool of private student loans ceded to AG Re by another monoline insurer. The guaranteed bonds were issued as auction rate securities that now bear a high rate of interest due to the downgrade of the primary insurer’s financial strength rating. Further, the underlying loan collateral has performed below expectations. Additionally, on another public student loan transaction reinsured from Ambac Assurance Corporation ("Ambac"), Ambac commuted its entire exposure during Second Quarter 2012. The Company's portion of the commutation payment was

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approximately $7 million, which was lower than expected. The overall decrease of approximately $2.7 million in net expected loss during Second Quarter 2012 is primarily due to the decrease in risk-free rates used to discount losses as well as an increase in the projected loss severities of certain transactions.

Trust Preferred Securities Collateralized Debt Obligations

The Company has insured or reinsured $1.7 billion of net par of collateralized debt obligations ("CDOs") backed by TruPS and similar debt instruments, or "TruPS CDOs." Of that amount, $745.1 million is rated BIG. The underlying collateral in the TruPS CDOs consists of subordinated debt instruments such as TruPS issued by bank holding companies and similar instruments issued by insurance companies, real estate investment trusts ("REITs") and other real estate related issuers.

The Company projects losses for TruPS CDOs by projecting the performance of the asset pools across several scenarios (which it weights) and applying the CDO structures to the resulting cash flows. At June 30, 2012, the Company has projected expected losses to be paid for TruPS CDOs that are accounted for as financial guaranty insurance of $6.5 million. The decrease of approximately $2.0 million in net expected loss during Second Quarter 2012 was driven primarily by a modest improvement in performance, which was partially offset by lower risk-free rates used to discount losses.

"XXX" Life Insurance Transactions

The Company's $2.3 billion net par of XXX life insurance transactions as of June 30, 2012 include $882.5 million rated BIG. The BIG "XXX" life insurance reserve securitizations are based on discrete blocks of individual life insurance business. In each such transaction the monies raised by the sale of the bonds 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.

The BIG "XXX" life insurance transactions consist of two transactions: Ballantyne Re p.l.c and Orkney Re II p.l.c. These transactions had material amounts of their assets invested in U.S. RMBS transactions. Based on its analysis of the information currently available, including estimates of future investment performance, and projected credit impairments on the invested assets and performance of the blocks of life insurance business at June 30, 2012, the Company's projected net expected loss to be paid is $135.3 million. The increase of $12.6 million during Second Quarter 2012 is due primarily to decreases in the risk-free rate used to discount losses and mild deterioration in the assets held by the trust, which was partially offset by the purchase of additional insured bonds for one of the transactions.

U.S. Public Finance Transactions

U.S. municipalities and related entities have been under increasing pressure over the last few quarters, and a few have filed for protection under the U.S. Bankruptcy Code, entered into state processes designed to help municipalities in fiscal distress or otherwise indicated they may consider not meeting their obligations to make timely payments on their debts. The Company expects that bondholder rights will be enforced. However, due to the early stage of these developments, and the circumstances surrounding each instance, the ultimate outcome cannot be certain. The Company will continue to analyze developments in each of these matters closely.

The Company has net exposure to Jefferson County, Alabama of $708.7 million. On November 9, 2011, Jefferson County filed for bankruptcy under Chapter 9 of the U.S. Bankruptcy Code in the U.S. Bankruptcy Court for the Northern District of Alabama (Southern Division).

Most of the Company's net exposure relates to $478.5 million in Jefferson County sewer revenue exposure, of which $205.4 million is direct and $273.1 million is assumed reinsurance exposure. The sewer revenue warrants are secured by a pledge of the net revenues of the sewer system. The bankruptcy court has affirmed that the net revenues constitute a “special revenue” under Chapter 9. Therefore, the net revenues of the sewer system are not subject to an automatic stay during the pendency of Jefferson County's bankruptcy case. BNY Mellon, as trustee, had brought a lawsuit regarding the amount of net revenues to which it is entitled. Since its bankruptcy filing, Jefferson County had been withholding estimated bankruptcy-related legal expenses and an amount representing a monthly reserve for future expenditures and depreciation and amortization from the monthly payments it had been making to the trustee from sewer revenues for debt service. On June 29, 2012 the Bankruptcy Court ruled that “Operating Expenses” as determined under the bond indenture do not include (1) a reserve for depreciation, amortization, or future expenditures, or (2) an estimate for professional fees and expenses, such that, after payment of Operating Expenses (as defined in the indenture), monies remaining in the Revenue Account created under the bond indenture must be distributed in accordance with the waterfall set forth in the indenture without withholding any monies for depreciation, amortization, reserves, or estimated expenditures that are the subject of this litigation. The court did

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not rule on whether actual incurred legal and professional fees constituted Operating Expenses that could be paid prior to debt service and Jefferson County filed a motion in July 2012 to clarify this point. Whether sufficient net revenues will be available for the payment of regularly scheduled debt service ultimately depends on the bankruptcy court's valuation of the sewer revenue stream.

The Company also has assumed exposure of $31.9 million to warrants that are payable from Jefferson County's general fund. During the past quarter Jefferson County chose not to make payment under its General Obligation bonds, so the Company has established a projected loss for these warrants as well. The Company's remaining net exposure of $198.3 million to Jefferson County relates to obligations that are secured by, or payable from, certain taxes that may have the benefit of a statutory lien or a lien on “special revenues” or other collateral.

On June 26, 2012, the City of Stockton filed for bankruptcy under Chapter 9 of the U.S. Bankruptcy Code due to drains on the general fund and projected deficits. The Company's net exposure to Stockton's general fund is $161.4 million, consisting of pension obligation and lease revenue bonds. As of June 30, 2012, the Company has paid $0.4 million in net claims.

The Company has $155.2 million of net par exposure to The City of Harrisburg, Pennsylvania, of which $94.9 million is BIG. The Company has paid $8.6 million in net claims to date, and expects a full recovery.

The Company projects that its total expected net loss from troubled U.S. public finance credits will be $58.4 million as of June 30, 2012, up from $32.7 million as of March 31, 2012. This increase was due primarily to changes in the interest and discount rates the Company uses to project cash flow related to the Jefferson County sewer revenue bonds and the establishment of expected losses related to the decision by Jefferson County not to make payments on its General Obligation bonds and the City of Stockton's filing for protection under Chapter 9 of the U.S. Bankruptcy Code.

Other Notable Transactions

The Company projects losses on, or is monitoring particularly closely, a number of other individual structured finance and international transactions, the most significant of which are described in the following paragraphs.

As of June 30, 2012 the Company had exposure to sovereign debt of Greece through financial guarantees of €200.0 million of debt (€165.1 million on a net basis) due in 2037 with a 4.5% fixed coupon and €114.3 million of inflation-linked debt (€52.7 million on a net basis) due in 2057 with a 2.085% coupon. On February 24, 2012, Greece announced the terms of exchange offers and consent solicitations that requested the voluntary participation by holders of certain Greek bonds, including the insured 2037 and 2057 bonds, in an exchange that resulted in the cancellation of such bonds in exchange for a package of replacement securities with lower principal amounts, and requested the consent of holders to amendments of the bonds that could be used to impose the same terms on holders that do not voluntarily participate in the exchange. In March 2012, the exchange was imposed through collective action clauses on the Company’s exposure to the 2037 bonds. In April 2012, the Company consented to the exchange with respect to its exposure on the 2057 bonds. The exchanges have caused the Company to recognize inception to date economic loss development of $311.7 million gross of reinsurance and $216.2 million, net of reinsurance and net of salvage received in the form of such exchanged securities, as of June 30, 2012. The Company recorded $15.6 million in gains due to changes in foreign exchange rates on its Greece reserve, which was recorded in other income. The Company accelerated claims under its financial guaranty on the July payment date with respect to the 2057 bonds and intends to accelerate claims on or after the September payment date with respect to the 2037 bonds.

The Company insures a total of $316.2 million net par of securities backed by manufactured housing loans, a total of $214.9 million rated BIG. The Company has expected loss to be paid of $21.4 million as of June 30, 2012 compared

to $18.4 million as of December 31, 2011 on two direct transactions from 2000-2001 with an aggregate net par of $137.1 million and one assumed transaction from 2001 with an aggregate net par of $4.8 million.

Recovery Litigation

RMBS Transactions

As of August 1, 2012, AGM and AGC have lawsuits pending on the following U.S. RMBS transactions insured by them. In the lawsuits, AGM and AGC have alleged breaches of R&W both in respect of the underlying loans in the transactions and the accuracy of the information provided to AGM and AGC, and failure to cure or repurchase defective loans identified by AGM and AGC to such persons:

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- ACE Securities Corp. Home Equity Loan Trust, Series 2006-GP1 (a second lien transaction in which AGM has sued Deutsche Bank AG affiliates DB Structured Products, Inc. and ACE Securities Corp.);

- Flagstar Home Equity Loan Trust, Series 2005-1 and Series 2006-2 (both second lien transactions in which AGM has sued Flagstar Bank, FSB, Flagstar Capital Markets Corporation and Flagstar ABS, LLC);

- SACO I Trust 2005-GP1 (a second lien transaction in which AGC has sued JPMorgan Chase & Co.'s affiliate EMC Mortgage LLC (formerly known as EMC Mortgage Corporation), J.P. Morgan Securities Inc. (formerly known as Bear, Stearns & Co. Inc.) and JPMorgan Chase Bank, N.A.);

- Bear Stearns Asset Backed Securities I Trust 2005-AC5 and Bear Stearns Asset Backed Securities I Trust 2005-AC6 (both first lien transactions in which AGC has sued EMC Mortgage LLC); and

- GMAC RFC Home Equity Loan-Backed Notes, Series 2006-HSA3 and GMAC Home Equity Loan-Backed Notes, Series 2004-HE3 (both second lien transactions in which AGM has sued GMAC Mortgage, LLC (formerly GMAC Mortgage Corporation; Residential Asset Mortgage Products, Inc.; Ally Bank (formerly GMAC Bank); Residential Funding Company, LLC (formerly Residential Funding Corporation); Residential Capital, LLC (formerly Residential Capital Corporation); Ally Financial (formerly GMAC, LLC); and Residential Funding Mortgage Securities II, Inc. On May 14, 2012, Residential Capital, LLC ("ResCap") and several of its affiliates (the "Debtors") filed for Chapter 11 protection with the U.S. Bankruptcy Court. The automatic stay of Bankruptcy Code Section 362 (a) stays lawsuits (such as the suit brought by AGM) against the Debtors. On May 25, 2012, ResCap filed an adversary proceeding in the United States Bankruptcy Court in the Southern District of New York against 42 defendants (including AGM) who are plaintiffs in 27 lawsuits arising from the Debtors' issuance or sale of mortgage backed securities (the "MBS Actions") that have asserted claims against non-debtor affiliates of ResCap. ResCap's adversary proceeding seeks declaratory relief or injunctive relief to extend the automatic stay to stay or enjoin the continuation of actions against the non-debtor affiliates based on the MBS Actions.

In these lawsuits, AGM and AGC seek damages, including indemnity or reimbursement for losses.

AGM also has a lawsuit pending in the Superior court of the State of California, County of Los Angeles, against UBS Securities LLC, as underwriter, as well as several named and unnamed control persons of IndyMac Bank, FSB and related IndyMac entities, that it filed in September 2010 on the IndyMac IMSC Mortgage Loan Trust, Series 2007-HOA-1a first lien transaction that it had insured, seeking damages for alleged violations of state securities laws and breach of contract, among other claims.

In October 2011, AGM and AGC brought an action in the Supreme Court of the State of New York against DLJ Mortgage Capital, Inc. ("DLJ") and Credit Suisse Securities (USA) LLC ("Credit Suisse") with regard to six first lien U.S. RMBS transactions insured by them:

- CSAB Mortgage-Backed Pass Through Certificates, Series 2006-2 (AGM insured);
- CSAB Mortgage-Backed Pass Through Certificates, Series 2006-3 (AGM insured);
- CSAB Mortgage-Backed Pass Through Certificates, Series 2006-4 (AGM insured);
- CMSC Mortgage-Backed Pass Through Certificates, Series 2007-3 (AGM insured);
- CSAB Mortgage-Backed Pass Through Certificates, Series 2007-1 (AGC insured); and
- TBW Mortgage-Backed Pass Through Certificates, Series 2007-2 (AGC insured).

The complaint alleges breaches of R&W by DLJ in respect of the underlying loans in the transactions, breaches of contract by DLJ and Credit Suisse in procuring falsely inflated shadow ratings (a condition to the issuance by AGC and AGM of its policies) by providing false and misleading information to the rating agencies, and failure by DLJ to

cure or repurchase defective loans identified by AGM and AGC.

In February 2012, AGM filed a complaint in the Supreme Court of the State of New York against UBS Real Estate Securities Inc. with respect to three first lien U.S. RMBS transactions it had insured:

- MASTR Adjustable Rate Mortgages Trust 2006-OA2;
- MASTR Adjustable Rate Mortgages Trust 2007-1; and
- MASTR Adjustable Rate Mortgages Trust 2007-3.

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The complaint alleges breaches of R&W by UBS Real Estate in respect of the underlying loans in the transactions, breaches of UBS Real Estate's repurchase obligations with respect to the defective loans identified by AGM, and breaches of contract by UBS Real Estate in procuring falsely inflated shadow ratings (a condition to the issuance by AGM of its policies) by providing false and misleading information to the rating agencies concerning the underlying loans in the transactions.

"XXX" Life Insurance Transactions

In December 2008, Assured Guaranty (UK) Ltd. ("AGUK") filed an action against J.P. Morgan Investment Management Inc. ("JPMIM"), the investment manager in the Orkney Re II transaction, in the Supreme Court of the State of New York alleging that JPMIM engaged in breaches of fiduciary duty, gross negligence and breaches of contract based upon its handling of the investments of Orkney Re II. 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. Separately, at the trial court level, discovery is ongoing.

Public Finance Transactions

In June 2010, AGM sued JPMorgan Chase Bank, N.A. and JPMorgan Securities, Inc. (together, "JPMorgan"), the underwriter of debt issued by Jefferson County, in the Supreme Court of the State of New York alleging that JPMorgan induced AGM to issue its insurance policies in respect of such debt through material and fraudulent misrepresentations and omissions, including concealing that it had secured its position as underwriter and swap provider through bribes to Jefferson County commissioners and others. In December 2010, the court denied JPMorgan's motion to dismiss. AGM has filed a motion with the Jefferson County bankruptcy court to confirm that continued prosecution of the lawsuit against JPMorgan will not violate the automatic stay applicable to Jefferson County notwithstanding JPMorgan's interpleading of Jefferson County into the lawsuit. AGM is continuing its risk remediation efforts for this exposure.

In September 2010, AGM, together with TD Bank, National Association and Manufacturers and Traders Trust Company, as trustees, filed a complaint in the Court of Common Pleas of Dauphin County, Pennsylvania against The Harrisburg Authority, The City of Harrisburg, Pennsylvania, and the Treasurer of the City in connection with certain Resource Recovery Facility bonds and notes issued by The Harrisburg Authority, alleging, among other claims, breach of contract by both The Harrisburg Authority and The City of Harrisburg, and seeking remedies including an order of mandamus compelling the City to satisfy its obligations on the defaulted bonds and notes and the appointment of a receiver for The Harrisburg Authority. Acting on its own, the City Council of Harrisburg filed a purported bankruptcy petition for the City in October 2011, which petition and a subsequent appeal were dismissed by the bankruptcy judge in November 2011. The City Council has appealed the dismissal of the appeal. As a result of the dismissal, the actions brought by AGM and the trustees against The City of Harrisburg and The Harrisburg Authority are no longer stayed. A receiver for The City of Harrisburg (the "City Receiver") was appointed by the Commonwealth Court of Pennsylvania in December 2011. The City Receiver filed a motion to intervene in the mandamus action and action for the appointment of a receiver for the resource recovery facility. In March 2012, the Court of Common Pleas of Dauphin County, Pennsylvania issued an order granting the motion for the appointment of a receiver for the resource recovery facility, which order has been appealed by The Harrisburg Authority.

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Net Loss Summary

The following table provides information on loss and LAE reserves net of reinsurance and salvage and subrogation recoverable on the consolidated balance sheets.

Loss and LAE Reserve (Recovery)
Net of Reinsurance and Salvage and Subrogation Recoverable

	As of June 30, 2012			As of December 31, 2011		
	Loss and LAE Reserve	Salvage and Subrogation Recoverable	Net	Loss and LAE Reserve	Salvage and Subrogation Recoverable	Net
	(in millions)					
U.S. RMBS:						
First lien:						
Prime first lien	$2.1	$—	$2.1	$1.2	$—	$1.2
Alt-A first lien	84.4	—	84.4	69.8	55.4	14.4
Option ARM	85.8	189.8	(104.0)	141.7	140.3	1.4
Subprime	71.8	0.3	71.5	51.4	0.3	51.1
Total first lien	244.1	190.1	54.0	264.1	196.0	68.1
Second lien:						
Closed-end second lien	13.9	67.1	(53.2)	11.2	136.2	(125.0)
HELOC	45.4	194.3	(148.9)	61.1	177.2	(116.1)
Total second lien	59.3	261.4	(202.1)	72.3	313.4	(241.1)
Total U.S. RMBS	303.4	451.5	(148.1)	336.4	509.4	(173.0)
TruPS	4.6	—	4.6	11.1	—	11.1
Other structured finance	192.4	6.6	185.8	221.9	5.9	216.0
U.S. public finance	108.2	75.2	33.0	62.2	69.9	(7.7)
Non-U.S. public finance	280.3	—	280.3	37.8	—	37.8
Total financial guaranty	888.9	533.3	355.6	669.4	585.2	84.2
Other	1.9	6.0	(4.1)	1.9	—	1.9
Subtotal	890.8	539.3	351.5	671.3	585.2	86.1
Effect of consolidating FG VIEs	(66.1)	(202.8)	136.7	(61.6)	(258.1)	196.5
Total (1)	$824.7	$336.5	$488.2	$609.7	$327.1	$282.6

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

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The following table reconciles the loss and LAE reserve and salvage and subrogation components on the consolidated balance sheet to the financial guaranty net reserves (salvage) in the financial guaranty BIG transaction loss summary tables.

Components of Net Reserves (Salvage)

	As of June 30, 2012	As of December 31, 2011
	(in millions)	
Loss and LAE reserve	$995.2	$ 679.0
Reinsurance recoverable on unpaid losses	(170.5)	(69.3)
Subtotal	824.7	609.7
Salvage and subrogation recoverable	(376.8)	(367.7)
Salvage and subrogation payable(1)	40.3	40.6
Subtotal	(336.5)	(327.1)
Total	488.2	282.6
Less: other	(4.1)	1.9
Financial guaranty net reserves (salvage)	$492.3	$ 280.7

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

The following table presents the loss and LAE recorded in the consolidated statements of operations by sector for financial guaranty insurance contracts. Amounts presented are net of reinsurance and net of the benefit for recoveries from breaches of R&W.

Loss and LAE Reported
on the Consolidated Statements of Operations

	Second Quarter		Six Months	
	2012	2011	2012	2011
	(in millions)			
Financial Guaranty:				
U.S. RMBS:				
First lien:				
Prime first lien	$0.5	$1.2	$0.9	$1.1
Alt-A first lien	29.0	19.2	27.7	27.4
Option ARM	16.9	70.4	69.4	41.3
Subprime	16.7	4.3	24.5	(5.1)
Total first lien	63.1	95.1	122.5	64.7
Second lien:				
Closed end second lien	2.4	(5.7)	1.6	(15.6)
HELOC	4.1	36.2	19.2	97.2
Total second lien	6.5	30.5	20.8	81.6
Total U.S. RMBS	69.6	125.6	143.3	146.3
TruPS	(1.8)	3.7	(6.1)	3.7
Other structured finance	29.3	7.4	1.2	27.7
U.S. public finance	25.3	3.4	44.5	(12.4)
Non-U.S. public finance	5.6	0.7	195.1	0.7
Total financial guaranty	128.0	140.8	378.0	166.0

Other	(6.0)	—	(6.0)	—
Subtotal	122.0	140.8	372.0	166.0
Effect of consolidating FG VIEs	0.5	(16.9)	(2.7)	(67.6)
Total loss and LAE	$122.5	$123.9	369.3	98.4

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

Financial Guaranty Insurance BIG Transaction Loss Summary
June 30, 2012

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating FG VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	164	(60)	79	(25)	132	(50)	375	—	375
Remaining weighted-average contract period (in years)	10.4	9.2	14.4	26.1	9.1	6.6	10.7	—	10.7
Outstanding exposure:									
Principal	$8,959.2	$(1,492.5)	$3,622.2	$(268.6)	$7,462.1	$(568.0)	$17,714.4	$—	$17,714.4
Interest	4,207.6	(563.4)	3,042.4	(504.0)	2,328.4	(157.0)	8,354.0	—	8,354.0
Total(2)	$13,166.8	$(2,055.9)	$6,664.6	$(772.6)	$9,790.5	$(725.0)	$26,068.4	$—	$26,068.4
Expected cash outflows (inflows)	$1,594.1	$(673.3)	$1,738.1	$(225.7)	$2,940.2	$(144.8)	$5,228.6	$(767.2)	$4,461.4
Potential recoveries(3)	(1,712.4)	696.1	(653.2)	20.3	(2,571.8)	122.0	(4,099.0)	805.4	(3,293.6)
Subtotal	(118.3)	22.8	1,084.9	(205.4)	368.4	(22.8)	1,129.6	38.2	1,167.8
Discount	18.6	(6.3)	(247.4)	29.4	(94.1)	(3.3)	(303.1)	27.5	(275.6)
Present value of expected cash flows	$(99.7)	$16.5	$837.5	$(176.0)	$274.3	$(26.1)	$826.5	$65.7	$892.2
Deferred premium revenue	$122.1	$(15.8)	$310.4	$(32.0)	$863.3	$(102.9)	$1,145.1	$(331.3)	$813.8
Reserves (salvage)(4)	$(132.5)	$23.2	$617.4	$(158.1)	$(0.4)	$6.0	$355.6	$136.7	$492.3

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Financial Guaranty Insurance BIG Transaction Loss Summary
December 31, 2011

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating FG VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	171	(68)	71	(26)	126	(48)	368	—	368
Remaining weighted-average contract period (in years)	10.0	9.2	13.7	20.5	9.2	6.4	10.4	—	10.4
Outstanding exposure:									
Principal	$9,675.8	$(1,378.0)	$3,731.6	$(274.0)	$7,830.8	$(627.7)	$18,958.5	$—	$18,958.5
Interest	4,307.9	(485.6)	2,889.4	(404.8)	2,486.4	(170.0)	8,623.3	—	8,623.3
Total(2)	$13,983.7	$(1,863.6)	$6,621.0	$(678.8)	$10,317.2	$(797.7)	$27,581.8	$—	$27,581.8
Expected cash outflows (inflows)	$1,730.6	$(658.8)	$1,833.3	$(120.3)	$2,423.0	$(133.4)	$5,074.4	$(998.4)	$4,076.0
Potential recoveries(3)	(1,798.0)	664.0	(1,079.3)	38.5	(2,040.5)	100.3	(4,115.0)	1,059.8	(3,055.2)
Subtotal	(67.4)	5.2	754.0	(81.8)	382.5	(33.1)	959.4	61.4	1,020.8
Discount	15.7	(4.6)	(240.6)	31.6	(125.1)	1.6	(321.4)	45.3	(276.1)
Present value of expected cash flows	$(51.7)	$0.6	$513.4	$(50.2)	$257.4	$(31.5)	$638.0	$106.7	$744.7
Deferred premium revenue	$260.8	$(69.1)	$280.9	$(12.3)	$991.8	$(126.6)	$1,325.5	$(390.7)	$934.8
Reserves (salvage)(4)	$(96.6)	$6.9	$319.5	$(41.9)	$(110.2)	$6.5	$84.2	$196.5	$280.7

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

(2) Includes BIG amounts related to FG VIEs which are not eliminated.

(3) Includes estimated future recoveries for breaches of R&W as well as excess spread, and draws on HELOCs.

(4) See table “Components of net reserves (salvage).”

The Company also has outstanding exposures to certain infrastructure transactions in its insured portfolio that may expose it to refinancing risk. These transactions generally involve long-term infrastructure projects that are financed by bonds that mature prior to the expiration of the project concession. While the cash flows from these projects were expected to be sufficient to repay all of the debt over the life of the project concession, in order to pay the principal on the early maturing debt, the Company expected it to be refinanced in the market at or prior to its maturity. Due to market dislocation and increased credit spreads, the Company may have to pay a claim at the maturity of the

securities, and then recover its payment 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 payments. The projected inflows and outflows are included in the Company's “Financial Guaranty Insurance BIG Transaction Loss Summary” table in this Note.

Ratings Impact on Financial Guaranty Business

A downgrade of one of the Company’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. Under the swaps, AGM insures periodic payments owed by the municipal obligors to the bank counterparties. Under certain of the swaps, 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

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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. The claim payments would be subject to recovery from the municipal obligor. As of June 30, 2012, taking into consideration whether the rating of the municipal obligor was below any applicable specified trigger as of such date, if the financial strength rating of AGM were 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 amount not exceeding $370.1 million in respect of such termination payments.

As another example, with respect to variable rate demand obligations ("VRDOs") for which a bank has agreed to provide a liquidity facility, a downgrade of AGM or AGC may provide the bank with the right to give notice to bondholders that the bank will terminate the liquidity facility, causing the bondholders to tender their bonds to the bank. Bonds held by the bank accrue interest at a “bank bond rate” that is higher than the rate otherwise borne by the bond (typically the prime rate plus 2.00% — 3.00%, and capped at the lesser of 25% and the maximum legal limit). In the event the bank holds such bonds for longer than a specified period of time, usually 90-180 days, the bank has the right to demand accelerated repayment of bond principal, usually through payment of equal installments over a period of not less than five years. In the event that a municipal obligor is unable to pay interest accruing at the bank bond rate or to pay principal during the shortened amortization period, a claim could be submitted to AGM or AGC under its financial guaranty policy. As of June 30, 2012, AGM and AGC has insured approximately $0.7 billion of par of VRDOs issued by municipal obligors rated BBB- or lower pursuant to the Company’s internal rating. For a number of such obligations, a downgrade of AGM or AGC below “A+” by S&P or below “A1” by Moody’s triggers the ability of the bank to notify bondholders of the termination of the liquidity facility and to demand accelerated repayment of bond principal over a period of 5 to 10 years. 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.

5. Fair Value Measurement

The Company carries the majority 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, constraints on liquidity and unobservable parameters. 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 Second Quarter 2012, 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 calculation 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 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 sources, while unobservable inputs

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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 within the fair value hierarchy is based on the lowest level of significant input to its valuation. All three levels require the use of observable market data when available.

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 beginning of the period when the transfer occurs. The Company reviews the classification between Levels 1, 2 and 3 quarterly to determine, based on the definitions provided, whether a transfer is necessary. During the periods presented, there were no transfers between Level 1 and Level 2 and no transfers in or out of Level 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 applications, which include available relevant market information, benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing. 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, listed in the approximate order of priority include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data and industry and economic events. 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. The vast majority of fixed maturities are classified as Level 2.

Short-term investments, that are traded in active markets, are classified within Level 1 in the fair value hierarchy and are 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.

Prices determined based upon model processes where at least one significant model assumption or input is unobservable, are considered to be Level 3 in the fair value hierarchy. At June 30, 2012, the Company used model processes to price 29 fixed maturity securities, which was 4% or $450.4 million of the Company's fixed-income securities and short-term investments at fair value. 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); house 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.

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Other Invested Assets

Other invested assets includes certain investments that are carried and measured at fair value on a recurring basis and non-recurring basis, as well as assets not carried at fair value. Within other invested assets, $76.8 million are carried at fair value on a recurring basis as of June 30, 2012. These assets primarily comprise certain short-term investments and fixed maturity securities classified as trading and are Level 2 in the fair value hierarchy. Also carried at fair value on a recurring basis are $1.4 million in notes classified as Level 3 in the fair value hierarchy. The fair value of these notes is determined by calculating the present value of the expected cash flows. The unobservable inputs used in the fair value measurement of the notes are discount rate, prepayment speed and default rate.

Within other invested assets, $8.4 million are carried at fair value on a non-recurring basis as of June 30, 2012. These assets are comprised of mortgage loans which are classified as Level 3 in the fair value hierarchy as there are significant unobservable inputs used in the valuation of such loans. The non-performing portion of these mortgage loans is valued using an average recovery rate. The performing loans are valued using management's determination of future cash flows arising from these loans, discounted at the rate of return that would be required by a market participant. The unobservable inputs used in the fair value measurement of the mortgage loans are discount rate, recovery on delinquent loans, loss severity, prepayment speed and default rate.

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 Securities") and AGM's Committed Preferred Trust Securities (the "AGM CPS Securities") agreements, and the estimated present value that the Company would hypothetically have to pay currently for a comparable security (see Note 13, Long Term Debt and Credit Facilities). The estimated current cost of the Company's CCS depends on several factors, including broker-dealer quotes for the outstanding securities, the U.S. dollar forward swap curve, London Interbank Offered Rate ("LIBOR")curve projections and the term the securities are estimated to remain outstanding.

Changes in fair value of the AGM CPS and AGC CCS securities were recorded in the consolidated statements of operations. As of June 30, 2012 these securities were classified as Level 3 in the fair value hierarchy because there is a reliance on significant unobservable inputs to the valuation model, including the broker-dealer quote and the Company's estimate of the term the securities will be outstanding. Prior to the third quarter 2011, the significant market inputs used were observable, therefore, the Company classified this fair value measurement as Level 2. The CCS were transferred to Level 3 on the fair value hierarchy in the third quarter of 2011 because the Company was no longer able to obtain the same level of pricing information as in past quarters.

Supplemental Executive Retirement Plans

The Company classifies the fair value measurement of the assets of the Company's various supplemental executive retirement plans as Level 1. 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.

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 that fall under derivative accounting standards requiring fair value accounting through the statement of operations. The

Company does not enter into CDS with the intent to trade these contracts and the Company may not unilaterally terminate a CDS contract; however, the Company has mutually agreed with various counterparties to terminate certain CDS transactions.

The terms of the Company's CDS contracts differ from more standardized credit derivative contracts sold by companies outside the financial guaranty industry. Management considers the non-standard terms of its credit derivative contracts in determining the fair value of these contracts. 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 to terminate certain CDS contracts.

Due to the lack of quoted prices for its instruments or for similar instruments, the Company determines the fair value of

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its credit derivative contracts primarily through modeling that uses various inputs to derive an estimate of the fair value of the Company's contracts in principal markets. Observable inputs other than quoted market prices exist; however, these inputs reflect contracts that do not contain terms and conditions similar to the credit derivative contracts issued by the Company. Management does not believe there is an established market where financial guaranty insured credit derivatives are actively traded. The terms of the protection under an insured financial guaranty credit derivative do not, except for certain rare circumstances, allow the Company to exit its contracts. 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 significantly 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 net premiums the Company expects to receive or pay for the credit protection under the contract and the estimated present value of premiums that a financial guarantor of comparable credit-worthiness would hypothetically charge or pay the Company 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 cash flows are the most readily observable inputs since they are based on the CDS contractual terms. These cash flows include premiums to be received or paid under the terms of the contract. Credit spreads capture the effect of recovery rates and performance of underlying assets of these contracts, among other factors. If credit spreads of the underlying obligations change, the fair value of the related credit derivative changes. Market liquidity also affects valuations of the underlying obligations. Market conditions at June 30, 2012 were such that market prices of the Company's CDS contracts were not available. Since market prices were not available, the Company used proprietary valuation models that used both unobservable and observable market data inputs as described under "Assumptions and Inputs" below. These models are primarily developed internally based on market conventions for similar transactions.

Valuation models include management estimates and current market information. Management is also required to make assumptions of how the fair value of credit derivative instruments is affected by current market conditions. 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 to determine the fair value of these credit derivative products, actual experience may differ from the estimates reflected in the Company's consolidated financial statements and the differences may be material.

Assumptions and Inputs

Listed below are various inputs and assumptions that are key to the establishment of the Company's fair value for CDS contracts.

· How gross spread is calculated: Gross spread is the difference between the yield of a security paid by an issuer on an insured versus uninsured basis or, in the case of a CDS transaction, the difference between the yield and

an index such as the LIBOR. Such pricing is well established by historical financial guaranty fees relative to the credit spread on risks assumed as observed and executed in competitive markets, including in financial guaranty reinsurance and secondary market transactions.

· How gross spread is allocated: Gross spread on a financial guaranty contract accounted for as CDS is allocated among:

1. the profit the originator, usually an investment bank, realizes for putting the deal together and funding the transaction ("bank profit");

2. premiums paid to the Company for the Company's credit protection provided ("net spread"); and

3. the cost of CDS protection purchased by the originator to hedge their counterparty credit risk exposure to the Company ("hedge cost").

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· The weighted average life which is based on expected remaining contractual cash flows and debt service schedules, which are readily observable inputs since they are based on the CDS contractual terms.

· The rates used to discount future expected losses.

The expected future premium cash flows for the Company's credit derivatives were discounted at rates ranging from 0.25% to 2.47% at June 30, 2012 and 0.30% to 2.70% at December 31, 2011.

Gross spread is used to ultimately determine the net spread a comparable financial guarantor would charge the Company to transfer its risk at the reporting date.The Company obtains gross spreads on risks assumed 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 spreads 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, the Company either interpolates or extrapolates CDS spreads 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.

· 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

	As of June 30, 2012		As of December 31, 2011	
Based on actual collateral specific spreads	5	%	5	%

Based on market indices	89	%	90	%
Provided by the CDS counterparty	6	%	5	%
Total	100	%	100	%

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

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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 an alternative 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 71%, as of June 30, 2012 and approximately 78% as of December 31, 2011 of our CDS contracts are fair valued using this minimum premium. 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 Company's contracts' contractual terms typically do not require the posting of collateral by the guarantor. The widening of a financial guarantor's own credit spread increases the cost to buy credit protection on the guarantor, thereby reducing the amount of premium the guarantor can capture out of the gross spread on the deal. The extent of the hedge depends on the types of instruments insured and the current market conditions.

A credit derivative asset on protection sold is the result of contractual cash flows 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 current 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.

Example

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.

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	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 Company premium received per annum (in bps)	40	22	%	10	2	%

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

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

In this example, the contractual cash flows (the Company premium received per annum above) exceed the amount a market participant would require the Company to pay in today's market to accept its obligations under the CDS contract, thus resulting in an asset. This credit derivative asset is equal to the difference in premium rates discounted at the corresponding LIBOR over the weighted average remaining life of the contract.

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.

· At June 30, 2012 and December 31, 2011, 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.

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 7, Consolidation of Variable Interest Entities.

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The FG VIEs that are consolidated by the Company issued securities collateralized by HELOCs, first lien and second lien RMBS, subprime automobile loans, and other loans and receivables. The lowest level input that is significant to the fair value measurement of these assets and liabilities in its entirety was a Level 3 input (i.e. unobservable), therefore management classified them as Level 3 in the fair value hierarchy. Prices were determined with the assistance of an independent third-party. The pricing is based on a discounted cash flow approach and the third-party's proprietary pricing models. 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); discount rates 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 for the FG VIE tranches insured by the Company, taking into account the timing of the potential default and the Company's own credit rating. These inputs are utilized to project the future cash flows of the security and to evaluate the overall bond profile. 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 algorithm's designed to aggregate market color, received by the third-party, on comparable bonds.

Changes in fair value of the FG VIEs' assets and liabilities are included in fair value gains (losses) on FG VIEs within the consolidated statement of operations. Except for net credit impairment that triggers a claim on the financial guaranty contract, the unrealized fair value adjustments related to the consolidated FG VIEs will reverse to zero over the terms of these financial instruments.

The fair value of the Company's FG VIE assets is sensitive to changes relating 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 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 uninsured VIE liabilities.

The fair value of the Company's insured FG VIE liabilities is also sensitive to changes relating to 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 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. In addition, the Company's insured FG VIE liabilities 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 FG VIE tranches insured by the Company. In general, when the timing of expected loss payments by the Company is extended into the future, this typically leads to a decrease in the value of the Company's insurance and a decrease in the fair value of the Company's insured FG VIE liabilities, 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 insured FG VIE liabilities.

Not Carried at Fair Value

Financial Guaranty Contracts in Insurance Form

The fair value of the Company's financial guaranty contracts accounted for as insurance was 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. This amount was based on the pricing assumptions management has observed for portfolio transfers that have occurred in the financial guaranty market and included 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 that are recorded within long-term debt was determined by calculating the present value of the expected cash flows. The Company uses a market approach to determine discounted future cash flows using market driven discount rates and a variety of assumptions, including LIBOR curve projections, 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

Assets Acquired in Refinancing Transactions

The fair value of the other invested assets was determined by calculating the present value of the expected cash flows. The Company uses a market approach to determine discounted future cash flows using market driven discount rates and a variety of assumptions, including LIBOR curve projections and prepayment and default assumptions. 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 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, 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 included in the tables below.

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of June 30, 2012

	Fair Value (in millions)	Fair Value Hierarchy Level 1	Level 2	Level 3
Assets:				
Investment portfolio, available-for-sale:				
Fixed maturity securities				
U.S. government and agencies	$828.1	$—	$828.1	$—
Obligations of state and political subdivisions	5,676.7	—	5,667.0	9.7
Corporate securities	1,032.1	—	1,032.1	—
Mortgage-backed securities:				
RMBS	1,395.6	—	1,228.9	166.7
Commercial mortgage-backed securities ("CMBS")	486.5	—	486.5	—
Asset-backed securities	488.3	—	214.3	274.0
Foreign government securities	300.2	—	300.2	—
Total fixed maturity securities	10,207.5	—	9,757.1	450.4
Short-term investments	919.8	62.8	857.0	—
Other invested assets(1)	85.2	—	75.4	9.8
Credit derivative assets	429.9	—	—	429.9
FG VIEs' assets, at fair value	2,726.0	—	—	2,726.0
Other assets(2)	67.2	23.0	—	44.2
Total assets carried at fair value	$14,435.6	$85.8	$10,689.5	$3,660.3
Liabilities:				
Credit derivative liabilities	$2,095.9	$—	$—	$2,095.9
FG VIEs' liabilities with recourse, at fair value	2,239.0	—	—	2,239.0
FG VIEs' liabilities without recourse, at fair value	1,042.3	—	—	1,042.3
Total liabilities carried at fair value	$5,377.2	$—	$—	$5,377.2

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Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2011

	Fair Value (in millions)	Fair Value Hierarchy Level 1	Level 2	Level 3
Assets:				
Investment portfolio, available-for-sale:				
Fixed maturity securities				
U.S. government and agencies	$922.4	$—	$922.4	$—
Obligations of state and political subdivisions	5,455.4	—	5,445.9	9.5
Corporate securities	1,038.4	—	1,038.4	—
Mortgage-backed securities:				
RMBS	1,427.9	—	1,294.3	133.6
CMBS	500.0	—	500.0	—
Asset-backed securities	458.1	—	222.6	235.5
Foreign government securities	339.7	—	339.7	—
Total fixed maturity securities	10,141.9	—	9,763.3	378.6
Short-term investments	734.0	210.3	523.7	—
Other invested assets(1)	43.5	—	32.8	10.7
Credit derivative assets	468.9	—	—	468.9
FG VIEs' assets, at fair value	2,819.1	—	—	2,819.1
Other assets(2)	79.5	25.7	—	53.8
Total assets carried at fair value	$14,286.9	$236.0	$10,319.8	$3,731.1
Liabilities:				
Credit derivative liabilities	$			