ASSURED GUARANTY LTD
Form 10-Q
November 07, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended September 30, 2014

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 November 3, 2014 was 161,989,034 (includes 47,747 unvested restricted shares).

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
Assured Guaranty Ltd.

Consolidated Balance Sheets (unaudited)

(dollars in millions except per share and share amounts)

	As of September 30, 2014	As of December 31, 2013
Assets		
Investment portfolio:		
Fixed-maturity securities, available-for-sale, at fair value (amortized cost of $10,019 and $9,488)	$10,485	$9,711
Short-term investments, at fair value	837	904
Other invested assets	127	170
Total investment portfolio	11,449	10,785
Cash	82	184
Premiums receivable, net of commissions payable	801	876
Ceded unearned premium reserve	420	452
Deferred acquisition costs	120	124
Reinsurance recoverable on unpaid losses	56	36
Salvage and subrogation recoverable	294	174
Credit derivative assets	86	94
Deferred tax asset, net	474	688
Financial guaranty variable interest entities' assets, at fair value	1,296	2,565
Other assets	291	309
Total assets	$15,369	$16,287
Liabilities and shareholders' equity		
Unearned premium reserve	$4,263	$4,595
Loss and loss adjustment expense reserve	760	592
Reinsurance balances payable, net	148	148
Long-term debt	1,303	816
Credit derivative liabilities	1,654	1,787
Current income tax payable	40	44
Financial guaranty variable interest entities' liabilities with recourse, at fair value	1,326	1,790
Financial guaranty variable interest entities' liabilities without recourse, at fair value	133	1,081
Other liabilities	388	319
Total liabilities	10,015	11,172
Commitments and contingencies (See Note 14)		
Common stock ($0.01 par value, 500,000,000 shares authorized; 164,580,427 and 182,177,866 shares issued and outstanding in 2014 and 2013)	2	2
Additional paid-in capital	2,035	2,466
Retained earnings	2,979	2,482
Accumulated other comprehensive income, net of tax of $148 and $71	333	160
Deferred equity compensation (320,193 and 320,193 shares)	5	5
Total shareholders' equity	5,354	5,115

Total liabilities and shareholders’ equity	$15,369	$16,287

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

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Assured Guaranty Ltd.

Consolidated Statements of Operations (unaudited)

(dollars in millions except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Revenues				
Net earned premiums	$144	$159	$412	$570
Net investment income	102	99	301	286
Net realized investment gains (losses):				
Other-than-temporary impairment losses	(17)	(3)	(47)	(20)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	4	5	(9)	0
Net impairment loss	(21)	(8)	(38)	(20)
Other net realized investment gains (losses)	2	1	13	43
Net realized investment gains (losses)	(19)	(7)	(25)	23
Net change in fair value of credit derivatives:				
Realized gains (losses) and other settlements	(14)	24	20	(44)
Net unrealized gains (losses)	269	330	127	(120)
Net change in fair value of credit derivatives	255	354	147	(164)
Fair value gains (losses) on committed capital securities	4	9	(11)	(4)
Fair value gains (losses) on financial guaranty variable interest entities	50	40	232	253
Other income (loss)	(11)	16	17	(5)
Total revenues	525	670	1,073	959
Expenses				
Loss and loss adjustment expenses	(44)	55	54	69
Amortization of deferred acquisition costs	4	4	12	8
Interest expense	27	21	67	63
Other operating expenses	50	54	165	166
Total expenses	37	134	298	306
Income (loss) before income taxes	488	536	775	653
Provision (benefit) for income taxes				
Current	36	67	75	125
Deferred	97	85	144	69
Total provision (benefit) for income taxes	133	152	219	194
Net income (loss)	$355	$384	$556	$459
Earnings per share:				
Basic	$2.10	$2.10	$3.15	$2.44
Diluted	$2.09	$2.09	$3.13	$2.43
Dividends per share	$0.11	$0.10	$0.33	$0.30

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

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Assured Guaranty Ltd.

Consolidated Statements of Comprehensive Income (unaudited)

(in millions)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income (loss)	$355	$384	$556	$459
Unrealized holding gains (losses) arising during the period on:				
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $4, $(1), $74 and $(99)	(5)	(11)	164	(280)
Investments with other-than-temporary impairment, net of tax provision (benefit) of $1, $(2), $(4) and $(17)	1	(2)	(8)	(34)
Unrealized holding gains (losses) arising during the period, net of tax	(4)	(13)	156	(314)
Less: reclassification adjustment for gains (losses) included in net income (loss), net of tax provision (benefit) of $(5), $(2), $(9) and $(4)	(10)	(3)	(19)	(4)
Change in net unrealized gains on investments	6	(10)	175	(310)
Other, net of tax provision	(5)	7	(2)	1
Other comprehensive income (loss)	$1	$(3)	$173	$(309)
Comprehensive income (loss)	$356	$381	$729	$150

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 Nine Months Ended September 30, 2014

(dollars in millions, except share data)

	Common Shares Outstanding	Common Stock Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Deferred Equity Compensation	Total Shareholders' Equity
Balance at December 31, 2013	182,177,866	$ 2	$2,466	$2,482	$ 160	$ 5	$5,115
Net income	—	—	—	556	—	—	556
Dividends ($0.33 per share)	—	—	—	(59)	—	—	(59)
Common stock repurchases	(18,025,594)	0	(438)	—	—	—	(438)
Share-based compensation and other	428,155	0	7	—	—	—	7
Other comprehensive income	—	—	—	—	173	—	173
Balance at September 30, 2014	164,580,427	$ 2	$2,035	$2,979	$ 333	$ 5	$5,354

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

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Assured Guaranty Ltd.

Consolidated Statements of Cash Flows (unaudited)

(in millions)

	Nine Months Ended September 30,	
	2014	2013
Net cash flows provided by (used in) operating activities	$347	$146
Investing activities		
Fixed-maturity securities:		
Purchases	(2,031)	(1,563)
Sales	951	812
Maturities	557	643
Net sales (purchases) of short-term investments	89	44
Proceeds from paydowns on financial guaranty variable interest entities’ assets	346	553
Other	9	81
Net cash flows provided by (used in) investing activities	(79)	570
Financing activities		
Dividends paid	(58)	(57)
Repurchases of common stock	(438)	(259)
Share activity under option and incentive plans	(1)	—
Paydowns of financial guaranty variable interest entities’ liabilities	(348)	(409)
Net proceeds from issuance of long-term debt	495	—
Repayment of long-term debt	(18)	(22)
Net cash flows provided by (used in) financing activities	(368)	(747)
Effect of exchange rate changes	(2)	(1)
Increase (decrease) in cash	(102)	(32)
Cash at beginning of period	184	138
Cash at end of period	$82	$106
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$68	$81
Interest	$45	$47

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)

September 30, 2014

1. Business and Basis of Presentation

Business

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

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

Basis of Presentation

The unaudited interim consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) and, in the opinion of management, reflect all adjustments that are of a normal recurring nature, necessary for a fair statement of the financial condition, results of operations and cash flows of the Company and its consolidated 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 September 30, 2014 and cover the three-month period ended September 30, 2014 ("Third Quarter 2014"), the three-month period ended September 30, 2013 ("Third Quarter 2013"), the nine-month period ended

September 30, 2014 ("Nine Months 2014") and the nine-month period ended September 30, 2013 ("Nine Months 2013"). Certain financial information that is normally included in annual financial statements prepared in accordance with GAAP, but is not required for interim reporting purposes, has been condensed or omitted. The year-end balance sheet data was derived from audited financial statements.

The unaudited interim consolidated financial statements include the accounts of AGL, its direct and indirect subsidiaries (collectively, the "Subsidiaries") and its consolidated FG VIEs. Intercompany accounts and transactions between and among all consolidated entities have been eliminated.

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, 2013, filed with the U.S. Securities and Exchange Commission (the "SEC").

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The Company's principal insurance company subsidiaries are:

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

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

2. Rating Actions

Rating Actions

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

In the last several years, Standard & Poor's Ratings Services ("S&P") and Moody's Investors Service, Inc. ("Moody's") have changed, multiple times, their financial strength ratings of the Company's insurance subsidiaries, or changed the outlook on such ratings. On July 22, 2013 Kroll Bond Rating Agency ("KBRA") assigned a rating of AA+ to MAC. The rating agencies' most recent actions and proposals related to AGL's insurance subsidiaries are:

- On March 18, 2014, S&P upgraded the financial strength ratings of all of AGL's insurance subsidiaries to AA (stable outlook) from AA- (stable outlook); it affirmed such ratings in a credit analysis issued on July 2, 2014.

- On July 2, 2014, Moody's affirmed the ratings of AGL and its subsidiaries, but changed to negative the outlook of the financial strength ratings of AGC and its subsidiary Assured Guaranty (UK) Ltd. ("AGUK").

- On July 15, 2014, Moody’s issued a “Request for Comment” on proposed changes to its credit rating methodology for financial guaranty insurance companies. While Moody’s noted that if changes to the credit rating methodology were adopted as proposed, Moody's does not expect to change outstanding ratings that it has assigned, there can be no assurance that the proposed changes will be adopted as proposed or that, even if they are, Moody’s would not change its ratings on AGM, AGC or AG Re.

- On August 4, 2014, KBRA affirmed MAC's AA+ (stable outlook) financial strength rating.

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

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

- Note 6, Financial Guaranty Insurance Losses
- Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives
- Note 13, Reinsurance and Other Monoline Exposures
- Note 15, Long Term Debt and Credit Facilities (regarding the impact on the Company's insured leveraged lease transactions)

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3. Outstanding Exposure

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

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

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

Surveillance Categories

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

The Company monitors its investment grade credits to determine whether any new credits need to be internally downgraded to BIG and refreshes its internal credit ratings on individual credits in quarterly, semi-annual or annual cycles based on the Company’s view of the credit’s quality, loss potential, volatility and sector. Ratings on credits in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter. The Company’s credit ratings on assumed credits are based on the Company’s reviews of low-rated credits or credits in volatile sectors, unless such information is not available, in which case, the ceding company’s credit rating of the transactions are used. The Company models the performance of many of its structured finance transactions as part of its periodic internal credit rating review of them. The Company models most assumed residential mortgage-backed security ("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 5, Expected Loss to be Paid, for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. For surveillance purposes, the Company calculates present value using a constant discount rate of 5%. (A risk-free rate is used for calculating the expected loss for financial statement purposes.)

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

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

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- BIG Category 2: Below-investment-grade transactions for which future 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 future losses are expected and on which claims (other than liquidity claims) have been paid.

Components of Outstanding Exposure

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

Financial Guaranty
Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding	
	September 30, 2014	December 31, 2013	September 30, 2014	December 31, 2013
	(in millions)			
Public finance	$605,569	$650,924	$569,974	$610,011
Structured finance	66,479	86,456	61,479	80,524
Total financial guaranty	$672,048	$737,380	$631,453	$690,535

In addition to the amounts shown in the table above, the Company’s net mortgage guaranty insurance debt service was approximately $140 million as of September 30, 2014 related to loans originated in Ireland and the U.K.

Financial Guaranty Portfolio by Internal Rating
As of September 30, 2014

Rating Category	Public Finance U.S. Net Par Outstanding	%	Public Finance Non-U.S. Net Par Outstanding	%	Structured Finance U.S Net Par Outstanding	%	Structured Finance Non-U.S Net Par Outstanding	%	Total Net Par Outstanding	%
	(dollars in millions)									
AAA	$4,173	1.3 %	$1,011	3.0 %	$23,193	51.7 %	$6,442	61.8 %	$34,819	8.3 %
AA	96,107	29.2	388	1.2	8,115	18.1	539	5.2	105,149	25.2
A	178,484	54.2	9,451	28.2	1,849	4.1	558	5.4	190,342	45.5
BBB	41,919	12.7	21,159	63.2	3,044	6.8	1,937	18.5	68,059	16.3
BIG	8,542	2.6	1,478	4.4	8,673	19.3	953	9.1	19,646	4.7
Total net par outstanding (excluding loss mitigation bonds)	$329,225	100.0 %	$33,487	100.0 %	$44,874	100.0 %	$10,429	100.0 %	$418,015	100.0 %
Loss Mitigation	29		—		1,260		—		1,289	

Bonds Net Par Outstanding (including loss mitigation bonds)	$329,254	$33,487	$46,134	$10,429	$419,304

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Financial Guaranty Portfolio by Internal Rating
As of December 31, 2013

Rating Category	Public Finance U.S. Net Par Outstanding	%	Public Finance Non-U.S. Net Par Outstanding	%	Structured Finance U.S Net Par Outstanding	%	Structured Finance Non-U.S Net Par Outstanding	%	Total Net Par Outstanding	%
	(dollars in millions)									
AAA	$4,998	1.4 %	$1,016	3.0 %	$32,317	54.9 %	$9,684	69.1 %	$48,015	10.5 %
AA	107,503	30.5	422	1.2	9,431	16.0	577	4.1	117,933	25.7
A	192,841	54.8	9,453	27.9	2,580	4.4	742	5.3	205,616	44.8
BBB	37,745	10.7	21,499	63.2	3,815	6.4	1,946	13.9	65,005	14.1
BIG	9,094	2.6	1,608	4.7	10,764	18.3	1,072	7.6	22,538	4.9
Total net par outstanding (excluding loss mitigation bonds)	$352,181	100.0%	$33,998	100.0%	$58,907	100.0%	$14,021	100.0%	$459,107	100.0%
Loss Mitigation Bonds	32		—		1,163		—		1,195	
Net Par Outstanding (including loss mitigation bonds)	$352,213		$33,998		$60,070		$14,021		$460,302	

In addition to amounts shown in the tables above, the Company had outstanding commitments to provide guaranties of $294 million for structured finance and $459 million for public finance obligations at September 30, 2014. The structured finance commitments include the unfunded component of pooled corporate and other transactions. Public finance commitments relate to primary and secondary public finance debt issuances. The expiration dates for the public finance commitments range between October 1, 2014 and February 25, 2017, with $335 million expiring prior to December 31, 2014. The commitments are contingent on the satisfaction of all conditions set forth in them and may expire unused or be canceled at the counterparty's request. Therefore, the total commitment amount does not necessarily reflect actual future guaranteed amounts.

Components of BIG Portfolio
Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of September 30, 2014

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
First lien U.S. RMBS:					
Prime first lien	$70	$266	$29	$365	$488
Alt-A first lien	601	653	658	1,912	2,986

Option ARM	18	58	118	194	700
Subprime	214	681	768	1,663	4,247
Second lien U.S. RMBS:					
Closed-end second lien	21	19	97	137	224
Home equity lines of credit (“HELOCs”)	1,306	17	283	1,606	1,817
Total U.S. RMBS	2,230	1,694	1,953	5,877	10,462
Trust preferred securities (“TruPS”)	1,175	—	343	1,518	4,549
Other structured finance	1,111	405	715	2,231	40,292
U.S. public finance	6,934	1,188	420	8,542	329,225
Non-U.S. public finance	891	587	—	1,478	33,487
Total	$12,341	$3,874	$3,431	$19,646	$418,015

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Components of BIG Net Par Outstanding
(Insurance and Credit Derivative Form)
As of December 31, 2013

	BIG Net Par Outstanding				Net Par
	BIG 1	BIG 2	BIG 3	Total BIG	Outstanding
			(in millions)		
First lien U.S. RMBS:					
Prime first lien	$52	$321	$30	$403	$541
Alt-A first lien	656	1,137	935	2,728	3,590
Option ARM	71	60	467	598	937
Subprime	297	908	740	1,945	6,130
Second lien U.S. RMBS:					
Closed-end second lien	8	20	118	146	244
HELOCs	1,499	20	378	1,897	2,279
Total U.S. RMBS	2,583	2,466	2,668	7,717	13,721
TruPS	1,587	135	—	1,722	4,970
Other structured finance	1,367	309	721	2,397	54,237
U.S. public finance	8,205	440	449	9,094	352,181
Non-U.S. public finance	1,009	599	—	1,608	33,998
Total	$14,751	$3,949	$3,838	$22,538	$459,107

BIG Net Par Outstanding
and Number of Risks
As of September 30, 2014

	Net Par Outstanding			Number of Risks(2)		
Description	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
	(dollars in millions)					
BIG:						
Category 1	$10,572	$1,769	$12,341	176	23	199
Category 2	2,786	1,088	3,874	79	19	98
Category 3	2,870	561	3,431	116	26	142
Total BIG	$16,228	$3,418	$19,646	371	68	439

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BIG Net Par Outstanding
and Number of Risks
As of December 31, 2013

Description	Net Par Outstanding Financial Guaranty Insurance(1)	Credit Derivative	Total	Number of Risks(2) Financial Guaranty Insurance(1)	Credit Derivative	Total
	(dollars in millions)					
BIG:						
Category 1	$12,391	$2,360	$14,751	185	25	210
Category 2	2,323	1,626	3,949	80	21	101
Category 3	3,031	807	3,838	119	27	146
Total BIG	$17,745	$4,793	$22,538	384	73	457

(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.

Exposure to the Selected European Countries

Several European countries continue to experience 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 European countries where the Company believes heightened uncertainties exist are: Greece, Hungary, Italy, Portugal and Spain (collectively, the “Selected European Countries”). The Company is closely monitoring its exposures in the Selected European Countries where it believes heightened uncertainties exist. Previously, the Company had included Ireland on this list but removed it during Third Quarter 2014 because of Ireland's strengthening economic performance and improving prospects; in 2014, Ireland's long-term foreign currency rating was upgraded one notch by S&P (to ‘A-’) and three notches by Moody’s (to ‘Baa1’). 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.

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Net Direct Economic Exposure to Selected European Countries(1)
As of September 30, 2014

	Hungary	Italy	Portugal	Spain	Total
	(in millions)				
Sovereign and sub-sovereign exposure:					
Non-infrastructure public finance (2)	$—	$929	$95	$250	$1,274
Infrastructure finance	327	15	11	140	493
Sub-total	327	944	106	390	1,767
Non-sovereign exposure:					
Regulated utilities	—	229	—	—	229
RMBS	197	280	—	—	477
Sub-total	197	509	—	—	706
Total	$524	$1,453	$106	$390	$2,473
Total BIG (See Note 5)	$524	$—	$106	$390	$1,020

(1) While the Company's exposures are shown in U.S. dollars, the obligations the Company insures are in various currencies, primarily Euros. 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) The exposure shown in the "Non-infrastructure 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.

When the Company directly insures an obligation, it assigns the obligation to a geographic location or locations based on its view of the geographic location of the risk. The Company may also have direct exposures to the Selected European Countries in business assumed from unaffiliated monoline insurance companies, in which case the Company depends upon geographic information provided by the primary insurer.

The Company has excluded from the exposure tables above its indirect economic exposure to the Selected European Countries through policies it provides on pooled corporate and commercial receivables transactions. The Company considers economic exposure to a selected European Country to be indirect when the exposure relates to only a small portion of an insured transaction that otherwise is not related to a Selected European Country. Total net indirect exposure to Selected European Countries in non-sovereign pooled corporate and non-sovereign commercial receivables is $425 million and $68 million, respectively, based on the proportion of the insured par equal to the proportion of obligors identified as being domiciled in a Selected European Country.

Exposure to Puerto Rico

The Company insures general obligation bonds of the Commonwealth of Puerto Rico and various obligations of its related authorities and public corporations aggregating $4.9 billion net par as of September 30, 2014. The Company rates $4.7 billion net par of that amount BIG.

Puerto Rico has experienced significant general fund budget deficits in recent years. These deficits have been covered primarily with the net proceeds of bond issuances, with interim financings provided by Government Development Bank for Puerto Rico ("GDB") and, in some cases, with onetime revenue measures or expense adjustment measures. In addition to high debt levels, Puerto Rico faces a challenging economic environment.

In June 2014, the Puerto Rico legislature passed the Puerto Rico Public Corporation Debt Enforcement and Recovery Act (the "Recovery Act") in order to provide a legislative framework for certain public corporations experiencing severe financial stress to restructure their debt. In its Quarterly Report dated as of July 17, 2014, the Commonwealth stated the Puerto

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Rico Electric Power Authority (“PREPA”) may need to seek relief under the Recovery Act due to liquidity constraints. In the same report, the Commonwealth disclosed PREPA utilized approximately $42 million on deposit in its reserve account in order to pay debt service due on its bonds on July 1, 2014. Investors in bonds issued by PREPA have filed suit in the United States District Court for the District of Puerto Rico asserting the Recovery Act violates the U.S. Constitution. On August 14, 2014, PREPA entered into forbearance agreements with the GDB, its bank lenders, and bondholders and financial guaranty insurers (including AGM and AGC) that hold or guarantee more than 60% of PREPA's outstanding bonds, in order to address its near-term liquidity issues. Creditors, including those who have challenged the constitutionality of the Recovery Act, agreed not to exercise available rights and remedies until March 31, 2015, and the bank lenders agreed to extend the maturity of two revolving lines of credit to the same date. PREPA agreed it would continue to make principal and interest payments on its outstanding bonds, and interest payments on its lines of credit, and would develop a five year business plan and a recovery program in respect of its operations.

Following the enactment of the Recovery Act, S&P, Moody’s and Fitch Ratings lowered the credit rating of the Commonwealth’s bonds and the ratings on certain of Puerto Rico’s public corporations. The Commonwealth disclosed its liquidity has been adversely affected by rating agency downgrades and by the limited market access for its debt. The Commonwealth noted it has relied on short-term financings and interim loans from the GDB and other private lenders, which reliance has constrained its liquidity and increased its near-term refinancing risk. The Commonwealth has also noted it is committed to addressing its fiscal and economic challenges and to repaying the general obligation debt of the Commonwealth and the debt of GDB and the public corporations that are not eligible to seek relief under the Recovery Act.

On October 30, 2014, legislation designed to stabilize the Puerto Rico Highway and Transportation Authority ("PRHTA") (“Bill 2212”) was introduced in the Commonwealth legislature. This bill provides for new tax revenues that will support PRHTA and requires the transfer of certain revenues from PHRTA to the Puerto Rico Infrastructure Finance Authority (“PRIFA”) in exchange for PRIFA assuming PRHTA’s debt obligations to GDB and amounts owed under its Bond Anticipation Notes. In addition, Bill 2212 provides for the transfer of operations of the Tren Urbano mass transit system to a new agency, which will reduce PRHTA’s future operating expenses. If the legislation is passed, GDB has indicated that this will allow PRHTA to become self-sufficient and avoid a restructuring through the Recovery Act.

Puerto Rico
Gross Par and Gross Debt Service Outstanding
As of September 30, 2014

	Gross Par Outstanding	Gross Debt Service Outstanding
	(in millions)	
Subject to the terms of the Recovery Act	$ 3,058	$ 5,328
Not subject to the terms of the Recovery Act	2,977	4,749
Total	$ 6,035	$ 10,077

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The following table shows the Company’s exposure to general obligation bonds of Puerto Rico and various obligations of its related authorities and public corporations.

Puerto Rico
Net Par Outstanding

	As of September 30, 2014		As of December 31, 2013	
	Total	Internal Rating	Total	Internal Rating
	(in millions)			
Exposures subject to the terms of the Recovery Act:				
PRHTA (Transportation revenue)	$ 844	BB-	$ 872	BB-
PREPA	772	B-	860	BB-
Puerto Rico Aqueduct and Sewer Authority	384	BB-	384	BB-
PRHTA (Highway revenue)	273	BB	302	BB
Puerto Rico Convention Center District Authority	174	BB-	185	BB-
Puerto Rico Public Finance Corporation				