Exhibit 99.1

Assured Guaranty Corp.

Consolidated Financial Statements

March 31, 2013

Assured Guaranty Corp.

Index to Consolidated Financial Statements

March 31, 2013

Assured Guaranty Corp.

Consolidated Balance Sheets (Unaudited)

(dollars in millions except per share and share amounts)

	As of March 31, 2013	As of December 31, 2012
Assets		
Investment portfolio:		
Fixed maturity securities, available-for-sale, at fair value (amortized cost of $2,537 and $2,543)	$ 2,702	$ 2,723
Short-term investments, at fair value	144	130
Other invested assets	33	63
Total investment portfolio	2,879	2,916
Cash	16	17
Premiums receivable, net of ceding commissions payable	244	250
Ceded unearned premium reserve	347	362
Reinsurance recoverable on unpaid losses	132	147
Salvage and subrogation recoverable	57	67
Credit derivative assets	471	388
Deferred tax asset, net	515	371
Financial guaranty variable interest entities' assets, at fair value	865	818
Other assets	144	174
Total assets	**$ 5,670**	**$ 5,510**
Liabilities and shareholder's equity		
Unearned premium reserve	$ 1,084	$ 1,125
Loss and loss adjustment expense reserve	255	308
Reinsurance balances payable, net	90	95
Note payable to affiliate	300	300
Credit derivative liabilities	2,033	1,512
Financial guaranty variable interest entities' liabilities with recourse, at fair value	506	484
Financial guaranty variable interest entities' liabilities without recourse, at fair value	399	374
Other liabilities	146	205
Total liabilities	**4,813**	**4,403**
Commitments and contingencies (See Note 14)		
Preferred stock ($1,000 liquidation preference, 200,004 shares authorized; none issued and outstanding)	—	—
Common stock ($720 par value, 500,000 shares authorized; 20,834 shares issued and outstanding)	15	15
Additional paid-in capital	1,037	1,037
Retained earnings (deficit)	(292)	(56)
Accumulated other comprehensive income, net of tax of $52 and $59	97	111
Total shareholder's equity	**857**	**1,107**
Total liabilities and shareholder's equity	**$ 5,670**	**$ 5,510**

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

Assured Guaranty Corp.

Consolidated Statements of Operations (Unaudited)

(in millions)

	Three Months Ended March 31,	
	2013	**2012**
Revenues		
Net earned premiums	$ 21	$ 20
Net investment income	22	25
Net realized investment gains (losses):		
Other-than-temporary impairment losses	(1)	(27)
Less: portion of other-than-temporary impairment loss recognized in other comprehensive income	1	(25)
Other net realized investment gains (losses)	22	1
Net realized investment gains (losses)	20	(1)
Net change in fair value of credit derivatives:		
Realized gains (losses) and other settlements	(3)	(52)
Net unrealized gains (losses)	(431)	(473)
Net change in fair value of credit derivatives	(434)	(525)
Fair value gain (loss) on committed capital securities	(6)	(9)
Fair value gains (losses) on financial guaranty variable interest entities	(5)	(6)
Other income	4	0
Total revenues	**(378)**	**(496)**
Expenses		
Loss and loss adjustment expenses	(16)	16
Amortization of deferred acquisition costs	(3)	2
Interest expense	4	4
Other operating expenses	19	20
Total expenses	**4**	**42**
Income (loss) before income taxes	**(382)**	**(538)**
Provision (benefit) for income taxes		
Current	(10)	1
Deferred	(136)	(193)
Total provision (benefit) for income taxes	**(146)**	**(192)**
Net income (loss)	**$ (236)**	**$ (346)**

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

Assured Guaranty Corp.

Consolidated Statements of Comprehensive Income (Unaudited)

(in millions)

	Three Months Ended March 31,	
	2013	2012
Net income (loss)	**$ (236)**	**$ (346)**
Unrealized holding gains (losses) arising during the period on:		
Investments with no other-than-temporary impairment, net of tax provision (benefit) of $(6) and $12	(8)	22
Investments with other-than-temporary impairment, net of tax provision (benefit) of $0 and $(9)	1	(16)
Unrealized holding gains (losses) arising during the period, net of tax	(7)	6
Less: reclassification adjustment for gains (losses) included in net income (loss)	1	(1)
Change in net unrealized gains on investments	(8)	7
Change in cumulative translation adjustment, net of tax provision (benefit) of $(1) and $1	(6)	1
Other comprehensive income (loss)	(14)	8
Comprehensive income (loss)	**$ (250)**	**$ (338)**

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

Assured Guaranty Corp.

Consolidated Statement of Shareholder's Equity (Unaudited)

For the Three Months Ended March 31, 2013

(in millions)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income	Total Shareholder's Equity
Balance, December 31, 2012	**$ —**	**$ 15**	**$ 1,037**	**$ (56)**	**$ 111**	**$ 1,107**
Net loss	—	—	—	(236)	—	(236)
Other comprehensive loss	—	—	—	—	(14)	(14)
Balance at March 31, 2013	**$ —**	**$ 15**	**$ 1,037**	**$ (292)**	**$ 97**	**$ 857**

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

Assured Guaranty Corp.

Consolidated Statements of Cash Flows (Unaudited)

(in millions)

	Three Months Ended March 31,	
	2013	2012
Net cash flows provided by (used in) operating activities	**$ (15)**	**$ (73)**
Investing activities		
Fixed maturity securities:		
Purchases	(168)	(39)
Sales	54	31
Maturities	110	47
Net sales (purchases) of short-term investments	(15)	10
Net proceeds from paydowns on financial guaranty variable interest entities' assets	21	19
Repayment of notes receivable from affiliate	4	46
Proceeds from sale of third party surplus notes	32	0
Net cash flows provided by (used in) investing activities	**38**	**114**
Financing activities		
Dividends paid	—	(15)
Net paydowns of financial guaranty variable interest entities' liabilities	(24)	(29)
Net cash flows provided by (used in) financing activities	**(24)**	**(44)**
Effect of exchange rate changes	0	2
Increase (decrease) in cash	(1)	(1)
Cash at beginning of period	17	31
Cash at end of period	**$ 16**	**$ 30**
Supplemental cash flow information		
Cash paid (received) during the period for:		
Income taxes	$ 28	$ (1)
Interest	$ —	$ —

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

1. Business and Basis of Presentation

Business

Assured Guaranty Corp. ("AGC" and, together with its subsidiaries, the "Company"), a Maryland domiciled insurance company, is an indirect and wholly-owned operating subsidiary of Assured Guaranty Ltd. ("AGL" and, together with its subsidiaries, "Assured Guaranty"). AGL 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.

AGC owns 100% of Assured Guaranty (UK) Ltd. ("AGUK"), a company incorporated in the United Kingdom ("U.K.") as a U.K. insurance company which AGC elected to place into runoff in October 2010. In addition, effective January 1, 2012, AGC formed a new wholly-owned subsidiary, AG PFC Holding LLC ("AGPFC"). AGPFC, which is a Delaware limited liability company, was formed in connection with loss mitigation efforts for a film library securitization transaction that AGC guarantees under a credit derivative contract in which its affiliate AG Financial Products Inc. ("AGFP") sold credit protection.

The Company applies 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 Company markets its credit protection products 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 in many countries, although its principal focus is on the U.S., as well as 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 public finance obligations and structured finance obligations. 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 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 includes within structured finance obligations 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, 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 March 31, 2013 and cover the three-month period ended March 31, 2013 ("First Quarter 2013") and the three-month period ended March 31, 2012 ("First Quarter 2012"). 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 AGC and its 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 Exhibit 99.1 in AGL's Form 8-K dated April 8, 2013, filed with the U.S. Securities and Exchange Commission (the “SEC”).

2. Business Changes 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.

Rating Actions

When a rating agency assigns a public rating to a financial obligation guaranteed by AGC or its subsidiary AGUK, it generally awards that obligation the same rating it has assigned to the financial strength of AGC or AGUK. Investors in products insured by AGC or AGUK 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, AGC and AGUK manage their business with the goal of achieving high financial strength ratings. If the financial strength ratings of AGC were reduced below current levels, AGC expects that could have adverse effects on its future business opportunities as well as the premiums it could charge for its insurance policies and consequently, a further downgrade could harm AGC's new business production and results of operations in a material respect. 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.

In the last several years, Standard and Poor’s Ratings Services (“S&P”) and Moody’s Investors Service, Inc. (“Moody’s”) have downgraded the financial strength ratings of AGC and AGUK. On January 17, 2013, Moody’s downgraded the Insurance Financial Strength ("IFS") ratings of AGC and AGUK from Aa3 to A3. While the outlook for the ratings from S&P and Moody's is stable, there can be no assurance that S&P and Moody's will not take further action on the Company's rating. For a discussion of the effect of rating actions by S&P or Moody's on the Company as of March 31, 2013, see the following:

- Note 6, Financial Guaranty Insurance Losses
- Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives

Accounting Changes

In 2013, the Company expanded Note 16, Other Comprehensive Income, upon adoption of new guidance on other comprehensive income disclosures.

Significant Transactions

On May 6, 2013, Assured Guaranty entered into an agreement with UBS Real Estate Securities Inc. and affiliates (the "UBS" Agreement) and a third party resolving the Assured Guaranty's claims and liabilities related to specified residential mortgage-backed securities ("RMBS") transactions that were issued, underwritten or sponsored by UBS and insured by Assured Guaranty Municipal Corp. ("AGM"), an affiliate of the Company, or AGC under financial guaranty insurance policies. The UBS Agreement did not have a monetary impact on AGC's financial results. See Note 5, Expected Loss to be Paid.

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, diversifying its insured portfolio and maintaining rigorous subordination or collateralization requirements on structured finance obligations. The Company also has utilized reinsurance by ceding business to third-party and affiliated 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 9, 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.

Debt Service Outstanding

	Gross Debt Service Outstanding		Net Debt Service Outstanding	
	March 31, 2013	December 31, 2012	March 31, 2013	December 31, 2012
	(in millions)			
Public finance	$ 144,570	$ 148,245	$ 101,717	$ 104,077
Structured finance	44,683	47,687	32,726	35,104
Total financial guaranty	$ 189,253	$ 195,932	$ 134,443	$ 139,181

Unless otherwise noted, ratings disclosed herein on the Company's insured portfolio reflect internal ratings. The Company'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 the Company in instances where the Company's AAA-rated exposure on its internal rating scale (which does not take into account the Company's financial guaranty) has additional credit enhancement due to either (1) the existence of another security rated AAA that is subordinated to the Company's exposure or (2) the Company'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 the Company's attachment point to be materially above the AAA attachment point.

Financial Guaranty Portfolio by Internal Rating
As of March 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)									
Super senior	$ —	—%	$ 703	19.8%	$ 3,756	15.3%	$ 1,704	27.8%	$ 6,163	6.7%
AAA	137	0.2	—	0.0	9,260	37.7	2,506	40.8	11,903	13.0
AA	8,590	15.0	259	7.3	2,471	10.1	138	2.3	11,458	12.5
A	37,128	64.7	1,122	31.6	897	3.5	187	3.1	39,334	43.0
BBB	10,425	18.2	1,284	36.2	1,886	7.7	1,080	17.6	14,675	16.0
Below-investment-grade ("BIG")	1,085	1.9	181	5.1	6,314	25.7	513	8.4	8,093	8.8
Total net par outstanding	$ 57,365	100.0%	$ 3,549	100.0%	$ 24,584	100.0%	$ 6,128	100.0%	$ 91,626	100.0%

Financial Guaranty Portfolio by Internal Rating
As of December 31, 2012

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)									
Super senior	$ —	—%	$ 741	19.8%	$ 3,937	15.1%	$ 1,949	28.1%	$ 6,627	7.0%
AAA	137	0.2	—	0.0	10,077	38.7	2,968	42.7	13,182	13.9
AA	8,680	14.9	277	7.4	1,975	7.6	143	2.1	11,075	11.6
A	37,367	64.2	1,209	32.4	1,485	5.7	346	5.0	40,407	42.5
BBB	10,976	18.8	1,326	35.5	2,175	8.3	987	14.2	15,464	16.3
BIG	1,094	1.9	184	4.9	6,424	24.6	549	7.9	8,251	8.7
Total net par outstanding	$ 58,254	100.0%	$ 3,737	100.0%	$ 26,073	100.0%	$ 6,942	100.0%	$ 95,006	100.0%

The Company classifies those portions of risks benefiting from reimbursement obligations collateralized, or expected to be collateralized, by eligible assets held in trust in acceptable reimbursement structures as the higher of 'AA' or their current internal rating.

Securities purchased for loss mitigation purposes, which are generally rated BIG, represented $329 million and $328 million of gross par outstanding as of March 31, 2013 and December 31, 2012, respectively.

In addition to amounts shown in the tables above, AGC had outstanding commitments to provide guaranties of $1.7 billion for structured finance and, together with AGM, up to $280 million for public finance obligations at March 31, 2013. 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 November 15, 2013 and February 25, 2017, with $141 million expiring prior to December 31, 2013. 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.

Economic 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 it believes heightened uncertainties exist are: Greece, Hungary, Ireland, Italy, Portugal and Spain (the "Selected European Countries"). The Company is closely monitoring its exposures in Selected European Countries where it believes heightened uncertainties exist. 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)
March 31, 2013

	Greece	Hungary (2)	Ireland	Italy	Portugal	Spain (2)	Total
				(in millions)			
Sovereign and sub-sovereign exposure:							
Public finance	$ —	$ —	$ —	$ —	$ —	$ 0	0
Infrastructure finance	—	27	17	49	62	21	176
Sub-total	—	27	17	49	62	21	176
Non-sovereign exposure:							
RMBS	—	3	—	—	—	—	3
Commercial receivables	—	1	10	42	11	2	66
Pooled corporate	16	—	70	129	2	286	503
Sub-total	16	4	80	171	13	288	572
Total	$ 16	$ 31	$ 97	$ 220	$ 75	$ 309	$ 748
Total BIG	$ —	$ 3	$ —	$ 2	$ 1	$ 9	$ 15

(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.

(2) See Note 5, Expected Loss to be Paid.

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. For direct exposure this can be a relatively straight-forward determination as, for example, a debt issue supported by availability payments for a toll road in a particular country. The Company may also assign portions of a risk to more than one geographic location. The Company may also have direct exposures to the Selected European Countries in business assumed from unaffiliated monoline insurance companies. In the case of assumed business for direct exposures, the Company depends upon geographic information provided by the primary insurer.

The Company has included in the exposure tables above its indirect economic exposure to the Selected European Countries through exposure it provides on (a) pooled corporate and (b) 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. In most instances, the trustees and/or servicers for such transactions provide reports that identify the domicile of the underlying obligors in the pool, although occasionally such information is not available to the Company. The Company has reviewed transactions through which it believes it may have indirect exposure to the Selected European Countries that is material to the transaction and included in the tables above the proportion of the insured par equal to the proportion of obligors so identified as being domiciled in a Selected European Country. The Company may also have indirect exposures to Selected European Countries in business assumed from unaffiliated monoline insurance companies. However, in the case of assumed business for indirect exposures, unaffiliated primary insurers generally do not provide such information to the Company.

There is a di mimimis exposure in the "Public Finance" category. 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. The Company understands that Moody's recently had undertaken a review of redenomination risk in selected countries in the Eurozone, including some of the Selected European Countries. No redenomination from the Euro to another currency has yet occurred and it may never occur. Therefore, it is not possible to be certain at this point how a redenomination of an issuer's obligations might be implemented in the future and, in particular, whether any redenomination would extend to the Company's obligations under a related financial guarantee.

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 5, Expected Loss to be Paid). 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 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.)

More extensive 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.

Financial Guaranty Exposures
(Insurance and Credit Derivative Form)
As of March 31, 2013

	BIG Net Par Outstanding				Net Par Outstanding	BIG Net Par as a % of Total Net Par Outstanding
	BIG 1	BIG 2	BIG 3	Total BIG		
			(in millions)			
First lien U.S. RMBS:						
Prime first lien	$ 20	$ 337	$ 4	$ 361	$ 395	0.4%
Alt-A first lien	69	1,280	604	1,953	2,558	2.1
Option ARM	53	284	102	439	598	0.5
Subprime	112	196	341	649	2,989	0.7
Second lien U.S. RMBS:						
Closed end second lien	—	34	39	73	135	0.1
Home equity lines of credit ("HELOCs")	2	—	313	315	325	0.3
Total U.S. RMBS	256	2,131	1,403	3,790	7,000	4.1
Trust preferred securities ("TruPS")	1,514	—	707	2,221	4,090	2.4
Other structured finance	302	124	390	816	19,622	0.9
U.S. public finance	574	282	229	1,085	57,365	1.2
Non-U.S. public finance	60	121	—	181	3,549	0.2
Total	$ 2,706	$ 2,658	$ 2,729	$ 8,093	$ 91,626	8.8%

Financial Guaranty Exposures
(Insurance and Credit Derivative Form)
As of December 31, 2012

	BIG Net Par Outstanding				Net Par Outstanding	BIG Net Par as a % of Total Net Par Outstanding
	BIG 1	BIG 2	BIG 3	Total BIG		
			(in millions)			
First lien U.S. RMBS:						
Prime first lien	$ 14	$ 355	$ 4	$ 373	$ 410	0.4%
Alt-A first lien	58	1,333	628	2,019	2,649	2.1
Option ARM	49	326	92	467	635	0.5
Subprime	57	176	349	582	3,104	0.6
Second lien U.S. RMBS:						
Closed end second lien	—	34	42	76	142	0.1
HELOCs	3	—	325	328	339	0.3
Total U.S. RMBS	181	2,224	1,440	3,845	7,279	4.0
TruPS	1,551	—	716	2,267	4,230	2.4
Other structured finance	349	118	394	861	21,506	0.9
U.S. public finance	588	261	245	1,094	58,254	1.2
Non-U.S. public finance	184	—	—	184	3,737	0.2
Total	$ 2,853	$ 2,603	$ 2,795	$ 8,251	$ 95,006	8.7%

Below-Investment-Grade Credits
By Category
As of March 31, 2013

Description	Net Par Outstanding			Number of Risks(2)		
	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
	(dollars in millions)					
BIG:						
Category 1	$ 1,449	$ 1,257	$ 2,706	72	27	99
Category 2	594	2,064	2,658	51	26	77
Category 3	1,415	1,314	2,729	61	19	80
Total BIG	$ 3,458	$ 4,635	$ 8,093	184	72	256

Below-Investment-Grade Credits
By Category
As of December 31, 2012

Description	Net Par Outstanding			Number of Risks(2)		
	Financial Guaranty Insurance(1)	Credit Derivative	Total	Financial Guaranty Insurance(1)	Credit Derivative	Total
	(dollars in millions)					
BIG:						
Category 1	$ 1,472	$ 1,381	$ 2,853	70	28	98
Category 2	591	2,012	2,603	50	25	75
Category 3	1,445	1,350	2,795	60	22	82
Total BIG	$ 3,508	$ 4,743	$ 8,251	180	75	255

(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 Premiums

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 a derivative under GAAP. Amounts presented in this note relate only to financial guaranty insurance contracts. See Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives, for a discussion of credit derivative revenues.

Net Earned Premiums

	First Quarter	
	2013	2012
	(in millions)	
Scheduled net earned premiums	$ 15	$ 17
Acceleration of premium earnings	5	4
Accretion of discount on net premiums receivable	1	(1)
Total net earned premiums(1)	$ 21	$ 20

(1) Excludes $0.3 million and $1 million in First Quarter 2013 and 2012, respectively, related to consolidated FG VIEs.

Net Unearned Premium Reserve Roll Forward

	First Quarter	
	2013	2012
	(in millions)	
Balance beginning of period	$ 763	$ 826
Premium written, net	(2)	8
Net premium earned, excluding accretion	(20)	(21)
Foreign exchange translation	(4)	2
Change in expected premium	0	9
Balance, end of period	$ 737	$ 824

Gross Premium Receivable, Net of Ceding Commissions Roll Forward

	First Quarter	
	2013	2012
	(in millions)	
Balance beginning of period	$ 250	$ 232
Premium written, net of ceding commissions	1	22
Premium payments received, net of ceding commissions	(9)	(32)
Adjustments:		
Changes in the expected term of financial guaranty insurance contracts	1	11
Accretion of discount, net of ceding commissions	3	(1)
Foreign exchange translation	(2)	0
Consolidation of FG VIEs	—	0
Other adjustments	—	2
Balance, end of period (1)	$ 244	$ 234

(1) Excludes $13 million and $11 million as of March 31, 2013 and 2012, 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 14% and 15% of installment premiums at March 31, 2013 and December 31, 2012, respectively, are denominated in currencies other than the U.S. dollar, primarily Euro and British Pound Sterling.

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

Expected Collections of Gross Premiums Receivable,
Net of Ceding Commissions (Undiscounted)

	March 31, 2013
	(in millions)
2013 (April 1 - June 30)	$ 19
2013 (July 1 - September 30)	7
2013 (October 1 - December 31)	7
2014	28
2015	25
2016	23
2017	20
2018-2022	85
2023-2027	50
2028-2032	26
After 2032	28
Total (1)	$ 318

(1) Excludes expected cash collections on FG VIEs of $17 million.

Scheduled Net Earned Premiums
Financial Guaranty Insurance Contracts

	As of March 31, 2013
	(in millions)
2013 (April 1 - June 30)	$ 15
2013 (July 1 - September 30)	15
2013 (October 1 - December 31)	15
Subtotal 2013	45
2014	60
2015	54
2016	50
2017	46
2018 - 2022	193
2023 - 2027	134
2028 - 2032	84
After 2032	71
Total present value basis(1)	737
Discount	34
Total future value	$ 771

(1) Excludes scheduled net earned premiums on consolidated FG VIEs of $11 million.

Selected Information for Policies Paid in Installments

	As of March 31, 2013	As of December 31, 2012
	(dollars in millions)	
Premiums receivable, net of ceding commission payable	$ 244	$ 250
Gross unearned premium reserve	228	234
Weighted-average risk-free rate used to discount premiums	3.7%	3.6%
Weighted-average period of premiums receivable (in years)	8.4	8.4

5. Expected Loss to be Paid

The following provides a summarized description of the three accounting models required under GAAP for each type of contract, with references to additional information provided throughout this report. The three models are insurance, derivative and VIE consolidation. This note provides information regarding expected claim payments to be made under all insured contracts regardless of form of execution.

Accounting Models:

Insurance Accounting

For contracts accounted for as financial guaranty insurance, loss and loss adjustment expenses ("LAE") reserve is recorded only to the extent and for the amount that expected losses to be paid exceed unearned premium reserve. As a result, the Company has expected losses that have not yet been expensed but will be expensed in future periods. Such amounts will be expensed in future periods as deferred premium revenue amortizes into income. Expected loss to be paid is important from a liquidity perspective in that it represents the present value of amounts that the Company expects to pay or recover in future periods. Expected loss to be expensed is important because it presents the Company's projection of incurred losses that will be recognized in future periods as deferred premium revenue amortizes into income. See Note 6, Financial Guaranty Insurance Losses.

Derivative Accounting, at Fair Value

For contracts that do not meet the financial guaranty scope exception in the derivative accounting guidance (primarily due to the fact that the insured is not required to be exposed to the insured risk throughout the life of the contract), the Company records such credit derivative contracts at fair value on the consolidated balance sheet with changes in fair value recorded in the consolidated statement of operations. Expected loss to be paid is an important measure used by management to analyze the net economic loss on credit derivatives. The fair value recorded on the balance sheet represents an exit price in a hypothetical market. The fair value is determined using significant Level 3 inputs in an internally developed model while the expected loss to be paid (which represents the present value of expected cash outflows) uses methodologies and assumptions consistent with financial guaranty insurance expected losses to be paid. See Note 7, Fair Value Measurement and Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives.

VIE Consolidation, at Fair Value

For financial guaranty insurance contracts issued on the debt of variable interest entities over which the Company is deemed to be the primary beneficiary due to its control rights, as defined in accounting literature, the Company consolidates the FG VIE. The Company's expected loss to be paid is a component of the fair value of the FG VIEs liabilities. The Company carries the assets and liabilities of the FG VIEs at fair value under the fair value option election. Management assesses the losses on the insured debt of the consolidated FG VIEs in the same manner as other financial guaranty insurance and credit derivative contracts. Expected loss to be paid for FG VIEs pursuant to AGC's financial guaranty insurance policies is calculated in a manner consistent with the Company's other financial guaranty insurance contracts.

Expected Loss to be Paid

The expected loss to be paid is equal to the present value of expected future cash outflows for claim and LAE payments, net of inflows for expected salvage and subrogation (i.e. excess spread on the underlying collateral, and estimated and contractual recoveries for breaches of representations and warranties), using current risk-free rates. When the Company becomes entitled to the cash flow from the underlying collateral of an insured credit under salvage and subrogation rights as a result of a claim payment or estimated future claim payment, it reduces the expected loss to be paid on the contract. Net expected loss to be paid is defined as expected loss to be paid, net of amounts ceded to reinsurers.

The current risk-free rate is based on the remaining period of the contract used in the premium revenue recognition calculation (i.e., the contractual or expected period, as applicable). The Company updates the discount rate each quarter and records the effect of such changes in economic loss development. Expected cash outflows and inflows are probability weighted cash flows that reflect the likelihood of all possible outcomes. The Company estimates the expected cash outflows and inflows using management's assumptions about the likelihood of all possible outcomes based on all information available to it. Those assumptions consider the relevant facts and circumstances and are consistent with the information tracked and monitored through the Company's risk-management activities.

Economic Loss Development

Economic loss development represents the change in expected loss to be paid attributable to all factors other than loss and LAE payments. It 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.

Loss Mitigation

Expected loss to be paid and economic loss development include the effects of loss mitigation strategies and other contractual rights to mitigate losses such as: recoveries for breaches of representations and warranties, and purchases of insured debt obligations. Additionally, in certain cases, issuers of insured obligations elected, or the Company and an issuer mutually agreed as part of a negotiation, to deliver the underlying collateral or insured obligation to the Company. In circumstances where the Company has acquired its own insured obligations that have expected losses, as part of loss mitigation strategy, expected loss to be paid is reduced by the proportionate share of the insured obligation that was purchased. The difference between the purchase price of the obligation and the fair value excluding the value of the Company's insurance, is treated as a paid loss. Assets that are purchased or put to the Company are recorded in the investment portfolio, at fair value, excluding the value of the Company's insurance or credit derivative contract. See Note 7, Fair Value Measurement and Note 10, Investments and Cash.

Loss Estimation Process

The Company’s loss reserve committee estimates expected loss to be paid for all contracts. Surveillance personnel present analyses related to potential losses to the Company’s loss reserve committee 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, those analyses 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 analyses 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 committee reviews and refreshes 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 all contracts, whether accounted for as insurance, credit derivatives or FG VIEs, by sector before and after the benefit for contractual and expected 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 3.72% as of March 31, 2013 and 0.0% to 3.28% as of December 31, 2012.

Net Expected Loss to be Paid,
Before Recoveries for Breaches of R&W
Roll Forward by Sector
First Quarter 2013

	Net Expected Loss to be Paid as of December 31, 2012	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid as of March 31, 2013(2)
		(in millions)		
U.S. RMBS:				
First lien:				
Prime first lien	$ 7	$ 3	$ —	$ 10
Alt-A first lien	324	(4)	(8)	312
Option ARM	105	1	(19)	87
Subprime	64	9	(2)	71
Total first lien	500	9	(29)	480
Second lien:				
Closed-end second lien	25	(1)	(2)	22
HELOCs	20	(2)	(2)	16
Total second lien	45	(3)	(4)	38
Total U.S. RMBS	545	6	(33)	518
TruPS	20	(1)	(1)	18
Other structured finance	113	3	(1)	115
U.S. public finance	22	(6)	(1)	15
Non-U.S. public finance	4	(1)	—	3
Total	$ 704	$ 1	$ (36)	$ 669

Net Expected Loss to be Paid,
Before Recoveries for Breaches of R&W
Roll Forward by Sector
First Quarter 2012

	Net Expected Loss to be Paid as of December 31, 2011	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid as of March 31, 2012
		(in millions)		
U.S. RMBS:				
First lien:				
Prime first lien	$ 3	$ —	$ —	$ 3
Alt-A first lien	331	15	(10)	336
Option ARM	147	6	(11)	142
Subprime	68	3	(1)	70
Total first lien	549	24	(22)	551
Second lien:				
Closed-end second lien	41	(2)	(5)	34
HELOCs	46	4	(13)	37
Total second lien	87	2	(18)	71
Total U.S. RMBS	636	26	(40)	622
TruPS	48	(3)	(1)	44
Other structured finance	111	(2)	(1)	108
U.S. public finance	21	18	(3)	36
Non-U.S. public finance	3	—	—	3
Total financial guaranty	$ 819	$ 39	$ (45)	$ 813

(1) Net of ceded paid losses, whether or not such amounts have been settled with reinsurers. Ceded paid losses are typically settled 45 days after the end of the reporting period. Such amounts are recorded in reinsurance recoverable on paid losses included in other assets.

(2) Includes expected LAE to be paid for mitigating claim liabilities of $8 million as of March 31, 2013 and $11 million as of December 31, 2012. The Company paid $3 million and $1 million in LAE for First Quarter 2013 and 2012, respectively.

Net Expected Recoveries from Breaches of R&W Rollforward First Quarter 2013

	Future Net R&W Benefit as of December 31, 2012	R&W Development and Accretion of Discount During First Quarter 2013	R&W Recovered During First Quarter 2013(1)	Future Net R&W Benefit as of March 31, 2013
	(in millions)			
U.S. RMBS:				
First lien:				
Prime first lien	$ 2	$ —	$ —	$ 2
Alt-A first lien	187	(7)	(5)	175
Option ARM	98	3	(5)	96
Total first lien	287	(4)	(10)	273
Second lien:				
Closed end second lien	19	—	(2)	17
HELOCs	18	—	—	18
Total second lien	37	—	(2)	35
Total	$ 324	$ (4)	$ (12)	$ 308

Net Expected Recoveries from Breaches of R&W Rollforward First Quarter 2012

	Future Net R&W Benefit as of December 31, 2011	R&W Development and Accretion of Discount During First Quarter 2012	R&W Recovered During First Quarter 2012(1)	Future Net R&W Benefit as of March 31, 2012
	(in millions)			
U.S. RMBS:				
First lien:				
Prime first lien	$ 2	$ —	$ —	$ 2
Alt-A first lien	172	18	—	190
Option ARM	84	2	—	86
Total first lien	258	20	—	278
Second lien:				
Closed end second lien	89	(1)	—	88
HELOCs	26	2	(9)	19
Total second lien	115	1	(9)	107
Total	$ 373	$ 21	$ (9)	$ 385

(1) Gross amounts recovered were $13 million and $12 million for First Quarter 2013 and 2012, respectively.

Net Expected Loss to be Paid,
After Net Expected Recoveries for Breaches of R&W
Roll Forward
First Quarter 2013

	Net Expected Loss to be Paid as of December 31, 2012	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid as of March 31, 2013
		(in millions)		
U.S. RMBS:				
First lien:				
Prime first lien	$ 5	$ 3	$ —	$ 8
Alt-A first lien	137	3	(3)	137
Option ARM	7	(2)	(14)	(9)
Subprime	64	9	(2)	71
Total first lien	213	13	(19)	207
Second lien:				
Closed-end second lien	6	(1)	—	5
HELOCs	2	(2)	(2)	(2)
Total second lien	8	(3)	(2)	3
Total U.S. RMBS	221	10	(21)	210
TruPS	20	(1)	(1)	18
Other structured finance	113	3	(1)	115
U.S. public finance	22	(6)	(1)	15
Non-U.S. public finance	4	(1)	—	3
Total financial guaranty	$ 380	$ 5	$ (24)	$ 361

Net Expected Loss to be Paid,
After Net Expected Recoveries for Breaches of R&W
Roll Forward
First Quarter 2012

	Net Expected Loss to be Paid as of December 31, 2011	Economic Loss Development	(Paid) Recovered Losses(1)	Net Expected Loss to be Paid as of March 31, 2012
		(in millions)		
U.S. RMBS:				
First lien:				
Prime first lien	$ 1	$ —	$ —	$ 1
Alt-A first lien	159	(3)	(10)	146
Option ARM	63	4	(11)	56
Subprime	68	3	(1)	70
Total first lien	291	4	(22)	273
Second lien:				
Closed-end second lien	(48)	(1)	(5)	(54)
HELOCs	20	2	(4)	18
Total second lien	(28)	1	(9)	(36)
Total U.S. RMBS	263	5	(31)	237
TruPS	48	(3)	(1)	44
Other structured finance	111	(2)	(1)	108
U.S. public finance	21	18	(3)	36
Non-U.S. public finance	3	—	—	3
Total financial guaranty	$ 446	$ 18	$ (36)	$ 428

(1) Net of ceded paid losses, whether or not such amounts have been settled with reinsurers. Ceded paid losses are typically settled 45 days after the end of the reporting period. Such amounts are recorded in reinsurance recoverable on paid losses included in other assets.

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

Net Expected Loss to be Paid
By Accounting Model
As of March 31, 2013

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives	Total
	(in millions)			
US RMBS:				
First lien:				
Prime first lien	$ 2	$ —	$ 6	$ 8
Alt-A first lien	25	8	104	137
Option ARM	(15)	—	6	(9)
Subprime	3	—	68	71
Total first lien	15	8	184	207
Second Lien:				
Closed-end second lien	(1)	6	—	5
HELOCs	(2)	—	—	(2)
Total second lien	(3)	6	—	3
Total U.S. RMBS	12	14	184	210
TruPS	1	—	17	18
Other structured finance	41	—	74	115
U.S. public finance	15	—	—	15
Non-U.S. public finance	3	—	—	3
Total	$ 72	$ 14	$ 275	$ 361

Net Expected Loss to be Paid
By Accounting Model
As of December 31, 2012

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives	Total
	(in millions)			
US RMBS:				
First lien:				
Prime first lien	$ 2	$ —	$ 3	$ 5
Alt-A first lien	25	9	103	137
Option ARM	(9)	—	16	7
Subprime	2	—	62	64
Total first lien	20	9	184	213
Second Lien:				
Closed-end second lien	(1)	7	—	6
HELOCs	2	—	—	2
Total second lien	1	7	—	8
Total U.S. RMBS	21	16	184	221
TruPS	1	—	19	20
Other structured finance	44	—	69	113
U.S. public finance	22	—	—	22
Non-U.S. public finance	4	—	—	4
Total	$ 92	$ 16	$ 272	$ 380

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

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

Net Economic Loss Development
By Accounting Model
First Quarter 2013

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
	(in millions)			
US RMBS:				
First lien:				
Prime first lien	$ —	$ —	$ 3	$ 3
Alt-A first lien	1	(1)	3	3
Option ARM	4	—	(6)	(2)
Subprime	—	—	9	9
Total first lien	5	(1)	9	13
Second Lien:				
Closed-end second lien	—	—	(1)	(1)
HELOCs	(2)	—	—	(2)
Total second lien	(2)	—	(1)	(3)
Total U.S. RMBS	3	(1)	8	10
TruPS	0	—	(1)	(1)
Other structured finance	(3)	—	6	3
U.S. public finance	(7)	—	1	(6)
Non-U.S. public finance	—	—	(1)	(1)
Total	$ (7)	$ (1)	$ 13	$ 5

Net Economic Loss Development
By Accounting Model
First Quarter 2012

	Financial Guaranty Insurance	FG VIEs(1)	Credit Derivatives(2)	Total
	(in millions)			
US RMBS:				
First lien:				
Prime first lien	$ —	$ —	$ —	$ —
Alt-A first lien	(4)	(2)	3	(3)
Option ARM	4	—	—	4
Subprime	—	—	3	3
Total first lien	—	(2)	6	4
Second Lien:				
Closed-end second lien	11	(12)	—	(1)
HELOCs	2	—	—	2
Total second lien	13	(12)	—	1
Total U.S. RMBS	13	(14)	6	5
TruPS	(3)	—	—	(3)
Other structured finance	(1)	—	(1)	(2)
U.S. public finance	17	—	1	18
Non-U.S. public finance	—	—	—	—
Total	$ 26	$ (14)	$ 6	$ 18

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

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

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 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 to the underlying mortgage loan files. Where the Company has an agreement with an R&W provider 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 certain scenarios included in the probability weighted R&W estimates for 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 Company's largest settlements. 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.

The ultimate performance of the Company's RMBS transactions remains highly uncertain, may differ from the Company's projections and may be subject to considerable volatility due to the influence of many factors, including the level and timing of loan defaults, changes in housing prices, results from the Company's loss mitigation activities and other variables. The Company will continue to monitor the performance of its RMBS exposures and will adjust its RMBS loss projection assumptions and scenarios based on actual performance and management's view of future performance.

First Quarter 2013 U.S. RMBS Loss Projections

The Company's RMBS loss projection methodology assumes that the housing and mortgage markets will eventually improve. Each quarter the Company makes a judgment as to whether to change the assumptions it uses to make RMBS loss projections based on its observation during the quarter of the performance of its insured transactions (including early stage delinquencies, late stage delinquencies and, for first liens, loss severity) as well as the residential property market and economy in general, and, to the extent it observes changes, it makes a judgment as whether those changes are normal fluctuations or part of a trend. Based on such observations, the Company chose to use essentially the same assumptions and scenarios to project RMBS loss as of March 31, 2013 as it used as of December 31, 2012 and as of December 31, 2011, except that, as compared to December 31, 2011:

- in its most optimistic scenario, it reduced by three months the period it assumed it would take the mortgage market to recover; and

- in its most pessimistic scenario, it increased by three months the period it assumed it would take the mortgage market to recover.

The Company's use of essentially the same assumptions and scenarios to project RMBS losses as of March 31, 2013 as at December 31, 2012 and December 31, 2011 was consistent with its view at March 31, 2013 that the housing and mortgage market recovery is occurring at a slower pace than it anticipated at December 31, 2012 or December 31, 2011. The Company's changes during 2012 to the period it would take the mortgage market to recover in its most optimistic scenario and its most pessimistic scenario resulted in a wider range of possibilities for the speed of the recovery. Since the Company's projections for each RMBS transaction are based on the delinquency performance of the loans in that individual RMBS transaction, improvement or deterioration in that aspect of a transaction's performance impacts the projections for that transaction. The methodology and assumptions the Company uses to project RMBS losses and the scenarios it employs are described in more detail below under "- 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".

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 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 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 range of key assumptions for the calculation of expected loss to be paid for individual transactions 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 March 31, 2013	As of December 31, 2012
Plateau CDR	6.9% - 9.0%	6.9% - 12.6%
Final CDR trended down to	0.5% - 2.2%	0.5% - 2.2%
Expected period until final CDR	36 months	36 months
Initial CPR	5.5% - 18.9%	4.9% - 15.4%
Final CPR	10%	10%
Loss severity	98%	98%
Initial draw rate	0.0% - 0.1%	0.0% - 0.2%

Closed-end second lien key assumptions	As of March 31, 2013	As of December 31, 2012
Plateau CDR	6.7% - 14.0%	7.3% - 14.3%
Final CDR trended down to	3.5% - 9.1%	3.5% - 9.1%
Expected period until final CDR	36 months	36 months
Initial CPR	2.9% - 13.4%	1.9% - 12.5%
Final CPR	10%	10%
Loss severity	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. The fifth month CDR is then used as the basis for the plateau period that follows the embedded five months of losses.

As of March 31, 2013, for the base case scenario, the CDR (the "plateau CDR") was held constant for one month. 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 used for December 31, 2012 and March 31, 2012. The long-term steady state CDR is 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 December 31, 2012.

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 (based on experience of the most recent three quarters) is assumed to continue until the end of the plateau before gradually increasing to the final CPR over the same period the CDR decreases. 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 December 31, 2012 and March 31, 2012. 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 be zero.

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.

As of March 31, 2013, 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 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 December 31, 2012. Increasing the CDR plateau to four months and increasing the ramp-down by three months to 33-months (for a total stress period of 42 months) would increase the expected loss by approximately $6 million for HELOC transactions and $0.5 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 (for a total stress period of 27 months) would decrease the expected loss by approximately $6 million for HELOC transactions and $0.5 million for closed-end second lien transactions. The length of the total stress period the Company used in its pessimistic scenario March 31, 2013 was the same as it used at December 31, 2012 but three months longer than the total stress period it used at March 31, 2012. On the other hand, the total stress period the Company used in its optimistic scenario at March 31, 2013 was the same as it used at December 31, 2012 but three months shorter than the total stress period it used at March 31, 2012.

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.

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 are one of the primary drivers of loss development in this portfolio. In order to determine the number of defaults resulting from these delinquent and foreclosed loans, the Company applies a liquidation rate assumption to loans in each of various delinquency categories. 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 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 Company projects these liquidations to occur over two years. For both First Quarter 2013 and

year-end 2012 the Company reviewed the data supplied by the third-party provider. Based on its review of that data, the Company maintained the same liquidation assumptions at March 31, 2013 as it had used at December 31, 2012. The following table shows liquidation assumptions for various delinquency categories.

First Lien Liquidation Rates

	March 31, 2013	December 31, 2012
30 – 59 Days Delinquent		
Alt-A and Prime	35%	35%
Option ARM	50	50
Subprime	30	30
60 - 89 Days Delinquent		
Alt-A and Prime	55	55
Option ARM	65	65
Subprime	45	45
90+ Days Delinquent		
Alt-A and Prime	65	65
Option ARM	75	75
Subprime	60	60
Bankruptcy		
Alt A and Prime	55	55
Option ARM	70	70
Subprime	50	50
Foreclosure		
Alt-A and Prime	85	85
Option ARM	85	85
Subprime	80	80
Real Estate Owned ("REO")		
All	100	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, after the initial 24-month CDR plateau period, each transaction's CDR is projected to improve over 12 months to an intermediate CDR (calculated as 20% of its CDR plateau); that intermediate CDR is held constant for 36 months and then trails off in steps to a final CDR of 5% of the CDR plateau. Under the Company's methodology, defaults projected to occur in the first 24 months represent 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. The CDR trend the Company used in its base case for March 31, 2013 was the same as it used for December 31, 2012 and December 31, 2011.

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 March 31, 2013 were the same as it used for December 31, 2012 and March 31, 2012. The Company then assumes that loss severities begin returning to levels

consistent with underwriting assumptions beginning in March 2014, and in the base case scenario, decline over two years to 40%.

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

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

	As of March 31, 2013	As of December 31, 2012
Alt-A First Lien		
Plateau CDR	3.7% - 18.4%	3.8% - 20.1%
Intermediate CDR	0.7% - 3.7%	0.8% - 4.0%
Final CDR	0.2% - 0.9%	0.2% - 1.0%
Initial loss severity	65%	65%
Initial CPR	1.6% - 39.6%	1.7% - 39.4%
Final CPR	15%	15%
Option ARM		
Plateau CDR	8.2% - 24.9%	7.6% - 26.0%
Intermediate CDR	1.6% - 5.0%	1.5% - 5.2%
Final CDR	0.4% - 1.2%	0.4% - 1.3%
Initial loss severity	65%	65%
Initial CPR	0.3% - 10.6%	0.0% - 10.7%
Final CPR	15%	15%
Subprime		
Plateau CDR	7.8% - 20.3%	7.3% - 21.2%
Intermediate CDR	1.6% - 4.1%	1.5% - 4.2%
Final CDR	0.4% - 1.0%	0.4% - 1.1%
Initial loss severity	90%	90%
Initial CPR	0.0% - 14.7%	0.0% - 17.6%
Final CPR	15%	15%

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

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. These assumptions are the same as those the Company used for December 31, 2012 and March 31, 2012.

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) as of March 31, 2013. For March 31, 2013 the Company used the same five scenarios and weightings as it used for December 31, 2012 and December 31, 2011 except that for March 31, 2013 it 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 assumed would be the case for December 31, 2011 and December 31, 2012. 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 $45 million for Alt-A first liens, $6 million for Option ARM, $18 million for subprime and $5 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 of 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 $119 million for Alt-A first liens, $23 million for Option ARM, $30 million for subprime and $15 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 $4 million for Alt-A first lien, $2 million for Option ARM, $3 million for subprime and $2 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 of March 31, 2012) expected loss to be paid would decrease from current projections by approximately $38 million for Alt-A first lien, $9 million for Option ARM, $13 million for subprime and $5 million for prime transactions.

Breaches of Representations and Warranties

Generally, when mortgage loans are transferred into a securitization, the loan originator(s) and/or sponsor(s) provide R&W, that the loans meet certain characteristics, and a breach of such R&W often requires that the loan be repurchased from the securitization. In many of the transactions the Company insures, it is in a position to enforce these requirements. The Company uses internal resources as well as third party forensic underwriting firms and legal firms to pursue breaches of R&W. If a provider of R&W refuses to honor its repurchase obligations, the Company may choose to initiate litigation. See "-Recovery Litigation" below.

The Company's success in pursuing R&W claims against a number of counterparties that provided R&W on a loan by loan basis has permitted the Company to pursue reimbursement agreements with R&W providers. Such agreements provide the Company with many of the benefits of pursuing the R&W claims but without the expense and uncertainty of pursuing the R&W claims on a loan by loan basis.

The Company has reached agreements with a number of R&W providers regarding their liabilities to Assured Guaranty relating to reimbursement for breaches of R&W and other matters. Through March 31, 2013, the Company has received $332 million (gross of reinsurance) pursuant to these agreements.

In consideration of payments, repurchases of mortgage loans and / or agreements to reimburse the Company in the future, the Company agreed to (among other things) release its claims for the repurchase of mortgage loans underlying the relevant transactions, so, except to the extent of future reimbursements pursuant to the relevant agreement, the Company retains at least a portion of the risk of future losses in the covered transactions. Importantly, a number of the agreements provide for future loss sharing payments, which are generally dependent on the future performance of the relevant transactions.

On May 6, 2013, Assured Guaranty entered into an agreement (the "UBS Agreement") with UBS and a third party resolving the Assured Guaranty's claims related to specified RMBS transactions that were issued, underwritten or sponsored by UBS and insured by AGM or AGC under financial guaranty insurance policies. Under the UBS Agreement, AGM received a cash payment of $358 million and UBS agreed to reimburse AGM for 85% of future losses on the MASTR Adjustable Rate Mortgages Trust 2006-OA2, MASTR Adjustable Rate Mortgages Trust 2007-1 and MASTR Adjustable Rate Mortgages Trust 2007-3 first lien RMBS transactions under a collateralized loss-sharing reinsurance agreement; that reinsurance arrangement is expected to be put in place by the third quarter of 2013. As of April 30, 2013, the aggregate par outstanding on these transactions was approximately $276.7 million. The UBS Agreement resolves all RMBS claims that Assured Guaranty has asserted against UBS in connection with these transactions, and also resolves the lawsuit AGM filed against UBS Securities LLC, as underwriter of the IndyMac IMSC Mortgage Loan Trust, Series 2007-HOA-1a first lien transaction, as well as potential Assured Guaranty claims on certain other UBS RMBS transactions not in litigation. The UBS Agreement did not have a monetary impact on AGC's financial results.

On May 8, 2012, Assured Guaranty reached an agreement ("Deutsche Bank Agreement") with Deutsche Bank AG and certain of its affiliates (collectively, "Deutsche Bank") regarding their liabilities relating to eight first and second lien transactions ("DB Covered Transactions"). As of March 31, 2013, the DB Covered Transactions have a gross par outstanding of $516 million ($444 million net of reinsurance).

- Under the Deutsche Bank Agreement, Deutsche Bank agreed (in addition to making payments since received by Assured Guaranty and other consideration) to reimburse Assured Guaranty for 80% of claims Assured Guaranty pays in the future on the DB Covered Transactions until the aggregate lifetime claims (before reimbursement) reach $319 million. As of March 31, 2013, Assured Guaranty was projecting in its base case that such aggregate lifetime claims would remain below $319 million. The Deutsche Agreement further requires Deutsche Bank to reimburse Assured Guaranty for 85% of the claims Assured Guaranty pays in the future on DB Covered Transactions to the extent aggregate lifetime claims (before reimbursement) are between $389 million and $600 million. Deutsche Bank is not required to reimburse Assured Guaranty for claims Assured Guaranty pays between the lifetime aggregates of $319 million and $389 million or to the extent they exceed $600 million. The two AGC Covered Transactions represented $89 million gross par outstanding ($75 million on a net basis) as of March 31, 2013.

- The Deutsche Bank Agreement also requires Deutsche Bank to reimburse Assured Guaranty for future claims it pays on certain RMBS re-securitizations that include uninsured tranches ("Uninsured Tranches") of the three DB Covered Transactions. Deutsche Bank is obligated to reimburse Assured Guaranty under the re-securitization transactions in an amount calculated as a percent of the losses in the Uninsured Tranches. That percent is 60% of losses up to $141 million and then from $161 million to $185 million and 100% from $185 million to $248 million. There is no reimbursement from $141 million to $161 million and above $248 million. As of March 31, 2013, Assured Guaranty was projecting in its base case that such losses would be $146 million.

- Deutsche Bank was required to place eligible assets in trust to collateralize its reimbursement obligation, and the amount it is required to post may be increased or decreased from time to time as determined by rating agency requirements. As of March 31, 2013 Deutsche Bank had placed $274 million of eligible assets in this trust account which, based on Assured Guaranty's projections, is sufficient to collateralize Deutsche Bank's obligations under the Deutsche Bank Agreement. Reimbursement payments are made quarterly and have been made timely.

- Except for the reimbursement obligation relating to the Uninsured Tranches, the Deutsche Bank Agreement does not include transactions where the Company has provided protection to Deutsche Bank on RMBS transaction in CDS form.

On April 14, 2011, Assured Guaranty reached an agreement ("Bank of America Agreement") with Bank of America Corporation and certain of its subsidiaries (collectively, "Bank of America") regarding their liabilities relating to first lien and second lien transactions. As of March 31, 2013, of the transactions insured by AGC, an aggregate of $0.9 billion gross par ($0.7 billion net of reinsurance) was outstanding. Under the Bank of America Agreement, Bank of America agreed (in addition to making payments since received by Assured Guaranty and other consideration) to reimburse Assured Guaranty for 80% of claims on the 21 first lien transactions Assured Guaranty pays in the future until the aggregate lifetime collateral losses (not insurance losses or claims) on those transactions reach $6.6 billion. As of March 31, 2013 aggregate lifetime collateral losses on those transactions was $3.3 billion, and Assured Guaranty was projecting in its base case that such collateral losses would eventually reach $5.1 billion. Bank of America has placed eligible assets in trust to collateralize its reimbursement obligation under the Bank of America Agreement;,the amount it is required to post may be increased or decreased from time to time as determined by rating agency requirements. As of March 31, 2013, Bank of America had placed $749 million of eligible assets in this trust account which, based on the Assured Guaranty's projections, should be sufficient to collateralize Bank of America's obligations under the Bank of America Agreement. Reimbursement payments are made monthly and have been made timely. Bank of America is not required to make any future reimbursements with respect to the second lien transactions covered by the Bank of America Agreement.

The Company uses the same RMBS projection scenarios and weightings to project the future benefit from the three settlement agreement described above as it uses to project RMBS losses on its portfolio. The Company accounts for the remaining loss sharing obligations under the Bank of America and Deutsche Bank Agreements as subrogation, offsetting the losses it projects by an R&W benefit from the relevant party for the applicable portion of the projected loss amount. To the extent the Company increases its loss projections, the R&W benefit under the Bank of America and Deutsche Bank Agreements will (subject to the limits described) also increase. Certain of the transactions covered by the various settlement agreements are also consolidated FG VIEs for which the R&W benefit is recorded at fair value. See Notes 7, Fair Value Measurement and 9, Consolidation of Variable Interest Entities.

Finally, based on its experience to date, the Company calculated an expected recovery from breaches of R&W in transactions not covered by agreements. 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 such 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 such contractual 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. 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.

The Company has included in its net expected loss estimates as of March 31, 2013 an estimated net benefit from loan repurchases related to breaches of R&W of $308 million, which includes $157 million from agreements with R&W providers and $151 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. 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 13,100 second lien and 800 first lien loan files (representing approximately $1 million and $0.3 million, respectively, of loans) in transactions as to which it eventually reached agreements. For the RMBS transactions as to which the Company had not settled its claims or won a judgment for breaches of R&W as of March 31, 2013, the Company had performed a detailed review of approximately 900 second lien and 9,300 first lien loan files, representing approximately $62 million of second lien and $3.3 billion of first lien 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 March 31, 2013 the Company has caused entities providing R&Ws to pay or agree to pay approximately $697 million (gross of reinsurance) in respect of their R&W liabilities for transactions in which the Company has provided a financial guaranty. Of this, $515 million are payments made or to be made pursuant to agreements with R&W providers and approximately $182 million are amounts paid into the relevant RMBS financial guaranty transactions pursuant to the transaction documents in the regular course.

The $515 million of payments made or to be made by R&W providers under agreements with the Company them includes $332 million that has already been received by the Company, as well as $183 million the Company projects receiving in the future pursuant to such currently existing agreements or judgment. Because much of that $183 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 $182 million paid by R&W providers were paid in the regular course into the relevant RMBS transactions in accordance with the priority of payments set out in the relevant transaction documents. 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.

U.S. RMBS Risks with R&W Benefit

	Number of Risks (1) as of		Debt Service as of	
	March 31, 2013	December 31, 2012	March 31, 2013	December 31, 2012
			(dollars in millions)	
Prime first lien	1	1	$ 17	$ 18
Alt-A first lien	18	16	2,215	2,271
Option ARM	3	3	393	417
Closed-end second lien	2	2	60	64
HELOC	1	1	17	18
Total	25	23	$ 2,702	$ 2,788

(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 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.

	First Quarter	
	2013	2012
	(in millions)	
Inclusion or removal of deals with breaches of R&W during period	$ 0	$ —
Change in recovery assumptions as the result of additional file review and recovery success	—	—
Estimated increase (decrease) in defaults that will result in additional (lower) breaches	(5)	11
Results of settlements	—	9
Accretion of discount on balance	1	1
Total	$ (4)	$ 21

The Company assumes that recoveries on second lien transactions that were not subject to the settlement agreements 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.

"XXX" Life Insurance Transactions

The Company's $746 million net par of XXX life insurance transactions as of March 31, 2013, include $279 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 March 31, 2013, the Company's projected net expected loss to be paid is $27 million. The overall decrease in expected loss to be paid of approximately $4 million is due primarily to the higher risk free rates used to discount the long dated projected losses in the transactions.

Student Loan Transactions

The Company has insured or reinsured $1.5 billion net par of student loan securitizations, of which $1.0 billion was issued by private issuers and classified as asset-backed and $0.5 billion was issued by public authorities and classified as public finance, of which $14 million is rated BIG. The Company is projecting approximately $1 million of net expected loss to be paid in these portfolios. In general, these losses are attributable to underlying loan collateral performing below expectations. There was no significant increase or decrease in net expected loss during First Quarter 2013.

Trust Preferred Securities Collateralized Debt Obligations

The Company has insured or reinsured $4.1 billion of net par (73% of which is in CDS form) of collateralized debt obligations ("CDOs") backed by TruPS and similar debt instruments, or "TruPS CDOs." Of that amount, $2.2 billion 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 March 31, 2013, the Company has projected expected losses to be paid for TruPS CDOs of $18 million. The decrease of approximately $2 million in net expected loss during First Quarter 2013 was driven primarily by the increase in risk free rates used for discounting as well as the increased valuation of certain assets in the TruPS pools.

Selected 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, given some 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 municipalities whose obligations the Company has insured that have filed for protection under Chapter 9 of the U.S Bankruptcy Code are: Jefferson County, Alabama and Stockton, California. The City Council of Harrisburg, Pennsylvania had also filed a purported bankruptcy petition, which was later dismissed by the bankruptcy court; a receiver for the City of Harrisburg was appointed by the Commonwealth Court of Pennsylvania on December 2, 2011.

The Company has assumed exposure to sewer revenue warrants issued by Jefferson County, Alabama of approximately $182 million as of March 31, 2013. On November 9, 2011, Jefferson County filed for bankruptcy under Chapter 9 of the U.S. Bankruptcy Code. Jefferson County and various parties holding and/or insuring the sewer revenue warrants have entered into agreements dated as of June 6, 2013 regarding a proposed Chapter 9 Plan to resolve the bankruptcy (the "Plan"). There are several conditions to the Plan becoming effective, including approval of the Plan by the court overseeing the bankruptcy. Should the Plan become effective, the Company's assumed sewer revenue exposure would be commuted for a net payment by the Company in connection with the Plan.

The Company has $8 million of net par exposure to The City of Harrisburg, Pennsylvania, all of which is BIG. The Company has paid $1 million in net claims as of March 31, 2013.

The Company has $249 million of net par exposure to the Louisville Arena Authority. The bond proceeds were used to construct the KFC Yum Center, home to the University of Louisville men's and women's basketball teams. Actual revenues available for Debt Service are well below original projections, and under the Company's internal rating scale, the transaction is BIG.

The Company has no remaining net par exposure to bonds secured by the excess free cash flow of the Foxwoods Casino, run by the Mashantucket Pequot Tribe. The Company had paid $4 million in net claims as of March 31, 2013 and expects full recovery of such amount.

The Company projects full or partial recovery on some of the claims it has already paid on its troubled U.S. public finance credits and that its total future expected net loss across its troubled U.S. public finance credits (after projected recoveries of claims already paid) will be $15 million as of March 31, 2013. This amount was a net loss of $22 million as of December 31, 2012. The decline in expected loss to be paid during the quarter was attributable primarily to developments in the bankruptcy settlement negotiation in Jefferson County, which caused the Company to attribute a higher probability to a scenario with a lower expected loss.

Certain Selected European Country Transactions

The Company reinsures credits with sub-sovereign exposure to various Spanish regions where a Spanish sovereign default causes the regions also to default. The Company's gross exposure to these credits is €19 million and its exposure net of reinsurance is €16 million. During 2012, the Company downgraded most of these exposures to the BB category due to concerns that these regions would not pay under their contractual obligations. The Company's Hungary exposure includes infrastructure

bonds dependent on payments from Hungarian governmental entities and a covered mortgage bond issued by a Hungarian bank. The Company's gross exposure to these credits is $40 million and its exposure net of reinsurance is $30 million of which $3 million is rated below investment grade. The Company estimated net expected losses of $0.4 million related to these Spanish and Hungarian credits, which has decreased slightly from December 31, 2012 largely due to the increased risk free rates used for discounting. Information regarding the Company's exposure to other Selected European Countries may be found under Note 3, Outstanding Exposure, –Economic Exposure to the Selected European Countries.

Manufactured Housing

The Company reinsures a total of $75 million net par of securities backed by manufactured housing loans, a total of $72 million rated BIG. The Company has expected loss to be paid of $11 million as of March 31, 2013 representing no change since December 31, 2012.

Infrastructure Finance

The Company has exposure to an infrastructure transaction with refinancing risk as to which the Company may need to make claim payments that it did not anticipate paying when the policy was issued; the aggregate amount of the claim payments may be substantial and reimbursement may not occur for an extended time, if at all. Total liabilities for one transaction with significant refinancing risk may amount to as much as $206 million, payable over the next 10 years. This transaction involves a long-term infrastructure project that is financed by bonds that mature prior to the expiration of the project concession. While the cash flows from the project 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. However, the recovery of the payments may take a long time and is uncertain. For the one transaction, the Company estimates that it may pay claims of $5 million, without giving effect to any payments that the Company may receive from reinsurers to which it has ceded a portion of this exposure. This estimate is based on certain assumptions the Company has made as to the performance of the transaction, including the refinancing of a certain portion of the debt, and the payment of certain anticipated contributions. The recoveries could take 35 years, depending on the performance of the underlying collateral.

Recovery Litigation

RMBS Transactions

As of the date of this filing, AGC has lawsuits pending against a number of providers of representations and warranties in U.S. RMBS transactions it has insured, seeking damages. In all the lawsuits, AGC has alleged breaches of R&W in respect of the underlying loans in the transactions and failure to cure or repurchase defective loans identified by AGC to such persons. In addition, in the lawsuit that AGC and its affiliate AGM filed against DLJ Mortgage Capital, Inc. (“DLJ”) and Credit Suisse Securities (USA) LLC (“Credit Suisse”), AGC and AGM have alleged breaches of contract 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.

- **J.P. Morgan**: AGC has sued JPMorgan Chase & Co.’s affiliate EMC Mortgage LLC ("EMC"), J.P. Morgan Securities Inc. (formerly known as Bear, Stearns & Co. Inc.) and JPMorgan Chase Bank, N.A. in the Supreme Court of the State of New York on the SACO I Trust 2005-GP1 second lien transaction and EMC Mortgage LLC in the United States District Court for the Southern District of New York on the Bear Stearns Asset Backed Securities I Trust 2005-AC5 and Bear Stearns Asset Backed Securities I Trust 2005-AC6 first lien transactions. On April 4, 2013, the Supreme Court of the State of New York ruled that AGC's sole remedy on its breach of contract claims is to compel EMC to repurchase defective loans, but allowed AGC to maintain its contractual reimbursement claim against EMC for its reasonable attorneys' fees and costs incurred in enforcing EMC's obligation to repurchase such loans. The Court also allowed AGC to pursue its repurchase claim against JP Morgan Securities, as an alter ego of EMC and successor to Bear Stearns & Co. As to the remaining claims, the Court (i) permitted AGC to bring a tortious-interference claim against JPMorgan Securities for instructing its subsidiary EMC to not repurchase defective loans, (ii) dismissed as premature AGC's breach of contract claim against EMC in respect of EMC's transfer of assets to JPMorgan without AGC's consent because AGC has not yet demonstrated actual damage from the breach, (iii) did not address or dismiss AGC's successor liability claim against JPMorgan Chase Bank, (iv) stated that it would postpone ruling on EMC's motion to dismiss AGC's fraud claim until after the New York appellate court rules on a similar motion in a separate litigation to which AGC is not a party.

- **Credit Suisse**: AGC and AGM have sued DLJ and Credit Suisse in the Supreme Court of the State of New York on first lien U.S. RMBS transactions insured by them. The ones insured by AGC are: CSAB Mortgage-Backed Pass Through Certificates, Series 2007-1 and TBW Mortgage-Backed Pass Through Certificates, Series 2007-2. On December 6, 2011, DLJ and Credit Suisse filed a motion to dismiss the cause of action asserting breach of the document containing the condition precedent regarding the rating of the securities and claims for recissionary damages and other relief in the complaint, and on October 11, 2012, the court granted the motion to dismiss. AGC and AGM intend to appeal the dismissal of certain of its claims. The causes of action against DLJ for breach of R&W and breach of its repurchase obligations remain.

"XXX" Life Insurance Transactions

In December 2008, 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.

6. Financial Guaranty Insurance Losses

Insurance Contracts' Loss Information

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

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

	As of March 31, 2013			As of December 31, 2012		
	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net	Loss and LAE Reserve, net	Salvage and Subrogation Recoverable, net	Net
	(in millions)					
U.S. RMBS:						
First lien:						
Prime first lien	$ 2	$ —	$ 2	$ 2	$ —	$ 2
Alt-A first lien	32	—	32	32	—	32
Option ARM	11	—	11	19	0	19
Subprime	2	—	2	3	0	3
Total first lien	47	—	47	56	0	56
Second lien:						
Closed-end second lien	1	—	1	2	0	2
HELOC	15	18	(3)	19	18	1
Total second lien	16	18	(2)	21	18	3
Total U.S. RMBS	63	18	45	77	18	59
TruPS	1	0	1	1	—	1
Other structured finance	36	5	31	44	6	38
U.S. public finance	29	26	3	46	35	11
Non-U.S. public finance	3	—	3	4	—	4
Subtotal	132	49	83	172	59	113
Effect of consolidating FG VIEs	(9)	—	(9)	(11)	—	(11)
Total(1)	$ 123	$ 49	$ 74	$ 161	$ 59	$ 102

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

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)
Insurance Contracts

	As of March 31, 2013	As of December 31, 2012
	(in millions)	
Loss and LAE reserve	$ 255	$ 308
Reinsurance recoverable on unpaid losses	(132)	(147)
Subtotal	123	161
Salvage and subrogation recoverable	(57)	(67)
Salvage and subrogation payable (1)	8	8
Subtotal	(49)	(59)
Other recoveries (2)	(26)	(29)
Subtotal	(75)	(88)
Financial guaranty net reserves (salvage)	$ 48	$ 73

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

(2) R&W recoveries recorded in other assets on the consolidated balance sheet.

Balance Sheet Classification of
Net Expected Recoveries for Breaches of R&W

	As of March 31, 2013			As of December 31, 2012		
	For all Financial Guaranty Insurance Contracts	Effect of Consolidating FG VIEs	Reported on Balance Sheet (1)	For all Financial Guaranty Insurance Contracts	Effect of Consolidating FG VIEs	Reported on Balance Sheet (1)
	(in millions)					
Salvage and subrogation recoverable	$ 44	$ —	$ 44	$ 46	$ —	$ 46
Loss and LAE reserve	92	(29)	63	97	(28)	69

(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 table below provides a reconciliation of net expected loss to be paid to net expected loss to be expensed. Expected loss to be paid differs from expected loss to be expensed due to: (1) 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 (2) loss reserves that have already been established (and therefore expensed but not yet paid).

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

	As of March 31, 2013 (in millions)
Net expected loss to be paid	$ 86
Less: net expected loss to be paid for FG VIEs	14
Total	72
Other recoveries (1)	26
Salvage and subrogation recoverable, net of reinsurance	49
Loss and LAE reserve, net of reinsurance	(123)
Net expected loss to be expensed (2)	$ 24

(1) R&W recoveries recorded in other assets on the consolidated balance sheet.

(2) Excludes $6 million as of March 31, 2013 related to consolidated FG VIEs.

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

Net Expected Loss to be Expensed Insurance Contracts

	As of March 31, 2013 (in millions)
2013 (April 1 - June 30)	$ 0
2013 (July 1 - September 30)	0
2013 (October 1–December 31)	1
Subtotal 2013	1
2014	2
2015	1
2016	1
2017	2
2018 - 2022	6
2023 - 2027	5
2028 - 2032	4
After 2032	2
Total present value basis(1)	24
Discount	25
Total future value	$ 49

(1) Consolidation of FG VIEs resulted in reductions of $6 million in net expected loss to be expensed.

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

Loss and LAE Reported
on the Consolidated Statements of Operations

	First Quarter	
	2013	2012
	(in millions)	
U.S. RMBS:		
First lien:		
Prime first lien	$ —	$ 0
Alt-A first lien	—	(6)
Option ARM	1	4
Subprime	—	0
Total first lien	1	(2)
Second lien:		
Closed end second lien	—	(1)
HELOC	(2)	2
Total second lien	(2)	1
Total U.S. RMBS	(1)	(1)
TruPS	—	(3)
Other structured finance	(5)	(1)
U.S. public finance	(11)	18
Non-U.S. public finance	—	—
Subtotal	(17)	13
Effect of consolidating FG VIEs	1	3
Total loss and LAE	$ (16)	$ 16

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

Financial Guaranty Insurance BIG Transaction Loss Summary
March 31, 2013

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	72	(28)	51	(14)	61	(24)	184	—	184
Remaining weighted-average contract period (in years)	12.6	11.9	13.9	13.9	12.3	14.2	12.2	—	12.2
Outstanding exposure:									
Principal	$ 1,884	$ (435)	$ 753	$ (159)	$ 2,421	$ (1,006)	$ 3,458	$ —	$ 3,458
Interest	993	(188)	634	(133)	679	(183)	1,802	—	1,802
Total(2)	$ 2,877	$ (623)	$ 1,387	$ (292)	$ 3,100	$ (1,189)	$ 5,260	$ —	$ 5,260
Expected cash outflows (inflows)	$ 27	$ (4)	$ 107	$ (16)	$ 1,028	$ (364)	$ 778	$ (117)	$ 661
Potential recoveries(3)	(29)	2	(37)	5	(739)	143	(655)	91	(564)
Subtotal	(2)	(2)	70	(11)	289	(221)	123	(26)	97
Discount	3	0	(22)	4	(121)	99	(37)	12	(25)
Present value of expected cash flows	$ 1	$ (2)	$ 48	$ (7)	$ 168	$ (122)	$ 86	$ (14)	$ 72
Unearned premium reserve	$ 14	$ (3)	$ 13	$ (2)	$ 24	$ (13)	$ 33	$ (7)	$ 26
Reserves (salvage)(4)	$ (7)	$ 0	$ 36	$ (4)	$ 151	$ (119)	$ 57	$ (9)	$ 48

Financial Guaranty Insurance BIG Transaction Loss Summary
December 31, 2012

	BIG Categories								
	BIG 1		BIG 2		BIG 3		Total BIG, Net	Effect of Consolidating VIEs	Total
	Gross	Ceded	Gross	Ceded	Gross	Ceded			
	(dollars in millions)								
Number of risks(1)	70	(27)	50	(16)	61	(23)	181	—	181
Remaining weighted-average contract period (in years)	13.0	11.9	13.9	13.7	12.6	14.9	12.5	—	12.5
Outstanding exposure:								—	
Principal	$ 1,925	$ (453)	$ 754	$ (163)	$ 2,454	$ (1,009)	$ 3,508	$ —	$ 3,508
Interest	1,065	(197)	622	(132)	705	(187)	1,876	—	1,876
Total(2)	$ 2,990	$ (650)	$ 1,376	$ (295)	$ 3,159	$ (1,196)	$ 5,384	$ —	$ 5,384
Expected cash outflows (inflows)	$ 28	$ (4)	$ 110	$ (18)	$ 1,021	$ (367)	$ 770	$ (121)	$ 649
Potential recoveries(3)	(29)	2	(34)	5	(747)	145	(658)	94	(564)
Subtotal	(1)	(2)	76	(13)	274	(222)	112	(27)	85
Discount	2	0	(20)	4	(74)	84	(4)	11	7
Present value of expected cash flows	$ 1	$ (2)	$ 56	$ (9)	$ 200	$ (138)	$ 108	$ (16)	$ 92
Unearned premium reserve	$ 15	$ (3)	$ 13	$ (3)	$ 22	$ (11)	$ 33	$ (7)	$ 26
Reserves (salvage)(4)	$ (7)	$ 0	$ 43	$ (6)	$ 186	$ (132)	$ 84	$ (11)	$ 73

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

(2) Includes BIG amounts related to FG VIEs.

(3) Includes 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)."

Ratings Impact on Financial Guaranty Business

A downgrade of AGC or AGUK may result in increased claims under financial guaranties issued by the Company if the insured obligors were unable to pay. For example, with respect to variable rate demand obligations ("VRDOs") for which a bank has agreed to provide a liquidity facility, a downgrade of 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 AGC under its financial guaranty policy. As of March 31, 2013, AGC has insured approximately $1.5 billion of net par of VRDOs, of which approximately $167 million of net par constituted VRDOs issued by municipal obligors rated BBB– or lower pursuant to the Company's internal rating. As of the date of this filing, the Company has not been notified that a bank has terminated a liquidity facility as result of the January 2013 Moody's downgrade, nor has there been a failed remarketing of the VRDOs, although in some cases, VRDOs insured by AGC have remarketed at higher interest rates. 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 AGC, vary depending on the transaction.

7. Fair Value Measurement

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

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

Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments include amounts to reflect counterparty credit quality, the Company's creditworthiness and constraints on liquidity. As markets and products develop and the pricing for certain products becomes more or less transparent, the Company may refine its methodologies and assumptions. During First Quarter 2013, 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 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.

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

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

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

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

Measured and Carried at Fair Value

Fixed Maturity Securities and Short-term Investments

The fair value of bonds in the investment portfolio is generally based on prices received from third party pricing services or alternative pricing sources with reasonable levels of price transparency. The pricing services prepare estimates of fair value measurements using their pricing 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. Benchmark yields have in many cases taken priority over reported trades for securities that trade less frequently. 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 March 31, 2013, the Company used model processes to price six fixed maturity securities, which was 3% or $84 million of the Company's fixed maturity 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.

Other Invested Assets

Within other invested assets, $8 million are carried at fair value on a recurring basis as of March 31, 2013. These assets primarily comprise certain short-term investments and fixed maturity securities classified as trading and are Level 2 in the fair value hierarchy.

Other Assets

Committed Capital Securities

The fair value of 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 the estimated present value that the Company would hypothetically have to pay currently for a comparable security (see Note 15, Note Payable to Affiliate 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.

Supplemental Executive Retirement Plans

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

Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company's credit derivatives consist primarily of insured CDS contracts 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 absent an event of default or termination event that entitles the Company to terminate; however, the Company has mutually agreed with various counterparties to terminate certain CDS transactions. Such terminations generally are completed for an amount that approximates the present value of future premiums, not at fair value.

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 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 importantly the Company's estimate of the value of the non-standard terms and conditions of its credit derivative contracts and of the Company's current credit standing.

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

The fair value of the Company's credit derivative contracts represents the difference between the present value of remaining premiums the Company expects to receive or pay 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. Consistent with the previous several quarters, market conditions at March 31, 2013 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.
- The allocation of gross spread 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").
- The weighted average life which is based on expected remaining contractual cash flows and Debt Service schedules.
- The rates used to discount future premium expected cash flows.

The expected future premium cash flows for the Company's credit derivatives were discounted at rates ranging from 0.2% to 3.0% at March 31, 2013 and 0.2% to 2.8% at December 31, 2012.

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 spread reflects a higher allocation to the cost of credit rather than the bank profit component. In the current market, it is assumed that a bank would be willing to accept a lower profit on distressed transactions in order to remove these transactions from its financial statements.

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

- Actual collateral specific credit spreads (if up-to-date and reliable market-based spreads are available).
- Deals priced or closed during a specific quarter within a specific asset class and specific rating.
- 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 March 31, 2013	As of December 31, 2012
Based on actual collateral specific spreads	12%	11%
Based on market indices	79%	80%
Provided by the CDS counterparty	9%	9%
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 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 close 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. For credit spreads on the Company's name the Company obtains the quoted price of CDS contracts traded on AGC from market data sources published by third parties. The cost to acquire CDS protection referencing AGC 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 increases, the amount of premium the Company retains on a deal generally decreases. As the cost to acquire CDS protection referencing AGC 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 31%, as of March 31, 2013 and approximately 64%, as of December 31, 2012 of the Company's CDS contracts are fair valued using this minimum premium. The change period over period is driven by AGC's credit spreads narrowing to levels not seen since 2008. As a result of this, the cost to hedge AGC's name has declined significantly causing more transactions to price above previously established floor levels.The Company corroborates the assumptions in its fair value model, including the portion of exposure to AGC hedged by its counterparties, with independent third parties each reporting period. The current level of AGC's own credit spread has resulted in the bank or deal originator hedging a significant portion of its exposure to AGC. This reduces the amount of contractual cash flows AGC 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 fair value resulting in a credit derivative asset on protection sold is the result of contractual cash inflows on in-force deals in excess of what a hypothetical financial guarantor could receive if it sold protection on the same risk as of the reporting date. If the Company were able to freely exchange these contracts (i.e., assuming its contracts did not contain proscriptions on transfer and there was a viable exchange market), it would be able to realize a gain representing the difference between the higher contractual premiums to which it is entitled and the current market premiums for a similar contract. The Company determines the fair value of its CDS contracts by applying the difference between the current net spread and the contractual net spread for the remaining duration of each contract to the notional value of its CDS contracts.

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.

	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 March 31, 2013 and December 31, 2012, 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.

As of March 31, 2013 these contracts were classified as Level 3 in the fair value hierarchy because there is a reliance on at least one unobservable input deemed significant to the valuation model, most significantly the Company's estimate of the value of non-standard terms and conditions of its credit derivative contracts and of amount of protection purchased on AGC's name.

Fair Value Option on FG VIEs' Assets and Liabilities

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

The FG VIEs that are consolidated by the Company issued securities collateralized by closed-end second lien RMBS, first lien RMBS, subprime 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 generally 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 (i.e. net expected loss to be paid as described in Note 5), the unrealized fair value gains (losses) 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 related to estimated prepayment speeds; estimated default rates (determined on the basis of an analysis of collateral attributes such as: historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); discount rates implied by market prices for similar securities; and house price depreciation/appreciation rates based on macroeconomic forecasts. Significant changes to some of these inputs could materially change the market value of the FG VIE's assets and the implied collateral losses within the transaction. In general, the fair value of the FG VIE asset is most sensitive to changes in the projected collateral losses, where an increase in collateral losses typically leads to a decrease in the fair value of FG VIE assets, while a decrease in collateral losses typically leads to an increase in the fair value of FG VIE assets. These factors also directly impact the fair value of the Company's FG VIE liabilities.

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

Not Carried at Fair Value

Financial Guaranty Insurance Contracts

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.

Note Payable to Affiliate

The fair value of the Company's note payable to affiliate is determined by calculating the present value of the expected cash flows. The Company determines discounted future cash flows using the effect of changes in U.S. Treasury yield at the end of each reporting period as well as the change in its own credit spread. The significant inputs were not readily observable. The Company accordingly classified this fair value measurement as Level 3.

Other Assets and Other Liabilities

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

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 March 31, 2013

	Fair Value	Fair Value Hierarchy		
		Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed maturity securities				
U.S. government and agencies	$ 478	$ —	$ 478	$ —
Obligations of state and political subdivisions	1,829	—	1,805	24
Corporate securities	140	—	140	—
Mortgage-backed securities:				
RMBS	69	—	37	32
Commercial mortgage-backed securities ("CMBS")	74	—	74	—
Asset-backed securities	28	—	0	28
Foreign government securities	84	—	84	—
Total fixed maturity securities	2,702	—	2,618	84
Short-term investments	144	106	38	—
Other invested assets	8	—	8	—
Credit derivative assets	471	—	—	471
FG VIEs' assets, at fair value	865	—	—	865
Other assets(1)	37	17	5	15
Total assets carried at fair value	$ 4,227	$ 123	$ 2,669	$ 1,435
Liabilities:				
Credit derivative liabilities	$ 2,033	$ —	$ —	$ 2,033
FG VIEs' liabilities with recourse, at fair value	506	—	—	506
FG VIEs' liabilities without recourse, at fair value	399	—	—	399
Total liabilities carried at fair value	$ 2,938	$ —	$ —	$ 2,938

Fair Value Hierarchy of Financial Instruments Carried at Fair Value
As of December 31, 2012

	Fair Value	Fair Value Hierarchy		
		Level 1	Level 2	Level 3
		(in millions)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed maturity securities				
U.S. government and agencies	$ 426	$ —	$ 426	$ —
Obligations of state and political subdivisions	1,860	—	1,837	23
Corporate securities	136	—	136	—
Mortgage-backed securities:				
RMBS	101	—	67	34
CMBS	82	—	82	—
Asset-backed securities	26	—	—	26
Foreign government securities	92	—	92	—
Total fixed maturity securities	2,723	—	2,640	83
Short-term investments	130	58	72	—
Other invested assets	23	—	23	—
Credit derivative assets	388	—	—	388
FG VIEs' assets, at fair value	818	—	—	818
Other assets(1)	40	14	5	21
Total assets carried at fair value	$ 4,122	$ 72	$ 2,740	$ 1,310
Liabilities:				
Credit derivative liabilities	$ 1,512	$ —	$ —	$ 1,512
FG VIEs' liabilities with recourse, at fair value	484	—	—	484
FG VIEs' liabilities without recourse, at fair value	374	—	—	374
Total liabilities carried at fair value	$ 2,370	$ —	$ —	$ 2,370

(1) Includes fair value of CCS and supplemental executive retirement plan assets.

Changes in Level 3 Fair Value Measurements

The table below presents a roll forward of the Company's Level 3 financial instruments carried at fair value on a recurring basis during First Quarter 2013 and 2012.

Fair Value Level 3 Rollforward
Recurring Basis
First Quarter 2013

	Fixed Maturity Securities							
	Obligations of State and Political Subdivisions	RMBS	Asset-Backed Securities	FG VIEs' Assets at Fair Value	Other Assets	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)							
Fair value at December 31, 2012	$ 23	$ 34	$ 26	$ 818	$ 21	$ (1,124)	$ (484)	$ (374)
Total pretax realized and unrealized gains/ (losses) recorded in:(1)								
Net income (loss)	0 (2)	0 (2)	0 (2)	68 (3)	(6) (4)	(434) (6)	(32) (3)	(39) (3)
Other comprehensive income(loss)	1	1	2	—	—	—	—	—
Settlements	—	(3)	0	(21)	—	(4)	10	14
FG VIE consolidations	—	—	—	—	—	—	—	—
Fair value as of March 31, 2013	$ 24	$ 32	$ 28	$ 865	$ 15	$ (1,562)	$ (506)	$ (399)
Change in unrealized gains/ (losses) related to financial instruments held as of March 31, 2013	$ 1	$ 1	$ 2	$ 82	$ (6)	$ (431)	$ (35)	$ (48)

Fair Value Level 3 Rollforward
Recurring Basis
First Quarter 2012

	Fixed Maturity Securities						
	RMBS	Asset-Backed Securities	FG VIEs' Assets at Fair Value	Other Assets	Credit Derivative Asset (Liability), net(5)	FG VIEs' Liabilities with Recourse, at Fair Value	FG VIEs' Liabilities without Recourse, at Fair Value
	(in millions)						
Fair value at December 31, 2011	$ 25	$ 6	$ 763	$ 31	$ (621)	$ (471)	$ (358)
Total pretax realized and unrealized gains/(losses) recorded in:(1)							
Net income (loss)	(1) (2)	0 (2)	27 (3)	(9) (4)	(525) (6)	(18) (3)	(19) (3)
Other comprehensive income (loss)	2	1	—	—	—	—	—
Purchases	—	—	—	—	(100) (7)	—	—
Settlements	(1)	—	(19)	—	45	13	16
FG VIE consolidations	—	—	7	—	—	(8)	—
Fair value as of March 31, 2012	$ 25	$ 7	$ 778	$ 22	$ (1,201)	$ (484)	$ (361)
Change in unrealized gains/(losses) related to financial instruments held as of March 31, 2012	$ 2	$ 1	$ 80	$ (9)	$ (473)	$ (24)	$ (53)

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

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

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

(4) Recorded in fair value gain (loss) on committed capital securities.

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

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

(7) Represents transferred ownership and assumed obligations related to a film securitization that AGC had previously guaranteed under a credit derivative contract.

Level 3 Fair Value Disclosures

Quantitative Information About Level 3 Fair Value Inputs
At March 31, 2013

Financial Instrument Description	Fair Value as of March 31, 2013 (in millions)	Valuation Technique	Significant Unobservable Inputs	Range
Assets:				
Fixed maturity securities:				
Obligations of state and	$ 24	Discounted cash	Rate of inflation	1.0% - 3.0%
political subdivisions		flow	Cash flow receipts	85.8%
			Yield	4.3% - 9.0%
			Collateral recovery period	1 month - 43 years
RMBS	32	Discounted cash	CPR	0.8% - 7.5%
		flow	CDR	8.3% - 12.1%
			Severity	50.5% - 71.3%
			Yield	3.7% - 9.3%
Asset-backed securities:				
XXX life insurance	28	Discounted cash	Yield	12.0%
transactions		flow		
FG VIEs' assets, at fair value	865	Discounted cash	CPR	1.0% - 11.0%
		flow	CDR	3.8% - 21.5%
			Loss severity	52.3% - 106.4%
			Yield	3.8% - 11.8%
Other assets	15	Discounted cash	Quotes from third party	
		flow	pricing	$51 - $53
			Term (in years)	3 years
Liabilities:				
Credit derivative liabilities, net	(1,562)	Discounted cash	Year 1 loss estimates	0.0% - 68.0%
		flow	Hedge cost (in bps)	14.8bps - 397.5bps
			Bank profit (in bps)	3.8bps - 1,336.5bps
			Internal floor (in bps)	7.0bps - 30.0bps
			Internal credit rating	AAA-BIG
FG VIEs' liabilities, at fair value	(905)	Discounted cash	CPR	1.0% - 11.0%
		flow	CDR	3.8% - 21.5%
			Loss severity	52.3% - 106.4%
			Yield	3.8% - 11.8%

Quantitative Information About Level 3 Fair Value Inputs
At December 31, 2012

Financial Instrument Description	Fair Value as of December 31, 2012 (in millions)	Valuation Technique	Significant Unobservable Inputs	Range
Assets:				
Fixed maturity securities:				
Obligations of state and	$ 23	Discounted cash	Rate of inflation	1.0% - 3.0%
political subdivisions		flow	Cash flow receipts	85.8%
			Discount rate	4.3% - 9.0%
			Collateral recovery period	1 month - 43 years
RMBS	34	Discounted cash	CPR	0.8% - 7.5%
		flow	CDR	8.3% - 22.3%
			Severity	48.1% - 101.3%
			Yield	5.8% - 9.9%
Asset-backed securities:				
XXX life insurance	26	Discounted cash	Yield	12.5%
transactions		flow		
FG VIEs' assets, at fair value	818	Discounted cash	CPR	1.0% - 10.9%
		flow	CDR	4.0% - 21.5%
			Loss severity	58.6% - 101.3%
			Yield	5.0% - 13.5%
Other assets	21	Discounted cash	Quotes from third party	
		flow	pricing	$38 - $48
			Term (in years)	3 years
Liabilities:				
Credit derivative liabilities, net	(1,124)	Discounted cash	Year 1 loss estimates	0.0% - 58.7%
		flow	Hedge cost (in bps)	67.5 - 678.4
			Bank profit (in bps)	3.8 - 1,312.9
			Internal floor (in bps)	7.0 - 30.0
			Internal credit rating	AAA - BIG
FG VIEs' liabilities, at fair value	(858)	Discounted cash	CPR	1.0% - 10.9%
		flow	CDR	4.0% - 21.5%
			Loss severity	58.6% - 101.3%
			Yield	5.0% - 13.5%

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

Fair Value of Financial Instruments

	As of March 31, 2013		As of December 31, 2012	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	(in millions)			
Assets:				
Fixed maturity securities	$ 2,702	$ 2,702	$ 2,723	$ 2,723
Short-term investments	144	144	130	130
Other invested assets	8	8	35	35
Credit derivative assets	471	471	388	388
FG VIEs' assets, at fair value	865	865	818	818
Other assets	66	66	70	70
Liabilities:				
Financial guaranty insurance contracts(1)	623	1,744	673	1,954
Note payable to affiliate	300	218	300	228
Credit derivative liabilities	2,033	2,033	1,512	1,512
FG VIEs' liabilities with recourse, at fair value	506	506	484	484
FG VIEs' liabilities without recourse, at fair value	399	399	374	374
Other liabilities	8	8	—	—

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

8. Financial Guaranty Contracts Accounted for as Credit Derivatives

The Company has a portfolio of financial guaranty contracts that meet the definition of a derivative in accordance with GAAP (primarily CDS). Until the Company ceased selling credit protection through credit derivative contracts in the beginning of 2009, following the issuance of regulatory guidelines that limited the terms under which the credit protection could be sold, management considered these agreements to be a normal part of its financial guaranty business. The potential capital or margin requirements that may apply under the Dodd-Frank Wall Street Reform and Consumer Protection Act contributed to the decision of the Company not to sell new credit protection through CDS in the foreseeable future.

Credit derivative transactions are governed by ISDA documentation and have different characteristics from financial guaranty insurance contracts. For example, the Company's control rights with respect to a reference obligation under a credit derivative may be more limited than when the Company issues a financial guaranty insurance contract. In addition, while the Company's exposure under credit derivatives, like the Company's exposure under financial guaranty insurance contracts, has been generally for as long as the reference obligation remains outstanding, unlike financial guaranty contracts, a credit derivative may be terminated for a breach of the ISDA documentation or other specific events. A loss payment is made only upon the occurrence of one or more defined credit events with respect to the referenced securities or loans. A credit event may be a non-payment event such as a failure to pay, bankruptcy or restructuring, as negotiated by the parties to the credit derivative transactions. If events of default or termination events specified in the credit derivative documentation were to occur, the non-defaulting or the non-affected party, which may be either the Company or the counterparty, depending upon the circumstances, may decide to terminate a credit derivative prior to maturity. The Company may be required to make a termination payment to its swap counterparty upon such termination. The Company may not unilaterally terminate a CDS contract; however, the Company on occasion has mutually agreed with various counterparties to terminate certain CDS transactions.

Credit Derivative Net Par Outstanding by Sector

The estimated remaining weighted average life of credit derivatives was 4.7 years at March 31, 2013 and 4.6 years at December 31, 2012. The components of the Company's credit derivative net par outstanding are presented below.

Credit Derivatives Net Par Outstanding

Asset Type	As of March 31, 2013 Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating	As of December 31, 2012 Net Par Outstanding	Original Subordination (1)	Current Subordination (1)	Weighted Average Credit Rating
	(dollars in millions)							
Pooled corporate obligations:								
Collateralized loan obligations/ collateralized bond obligations	$ 9,225	36.3%	37.2%	AAA	$ 10,597	37.2%	37.0%	AAA
Synthetic investment grade pooled corporate	430	30.0	29.1	AAA	430	30.0	29.1	AAA
TruPS CDOs	3,006	46.8	33.1	BB	3,100	46.9	32.4	BB
Market value CDOs of corporate obligations	1,621	40.7	33.0	AAA	1,583	41.3	33.9	AAA
Total pooled corporate obligations	14,282	38.8	35.6	AA+	15,710	39.4	35.6	AA+
U.S. RMBS:								
Option ARM and Alt-A first lien	2,503	20.1	10.2	B+	2,597	20.2	10.4	B+
Subprime first lien	2,594	29.9	52.5	AA-	2,698	29.8	52.6	A+
Prime first lien	266	10.9	5.2	B	277	10.9	5.2	B
HELOCs	5	—	—	A	6	—	—	A+
Total U.S. RMBS	5,368	24.2	30.2	BBB	5,578	24.2	30.4	BBB
CMBS	3,147	33.3	42.0	AAA	3,238	33.3	41.8	AAA
Other	3,748	—	—	A	3,883	—	—	A
Total	$ 26,545			AA-	$ 28,409			AA

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

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

The Company's TruPS CDO asset pools are generally less diversified by obligors and industries than the typical CLO asset pool. Also, the underlying collateral in TruPS CDOs consists primarily of subordinated debt instruments such as TruPS issued by bank holding companies and similar instruments issued by insurance companies, REITs and other real estate related issuers while CLOs typically contain primarily senior secured obligations. However, to mitigate these risks, TruPS CDOs were typically structured with higher levels of embedded credit enhancement than typical CLOs.

The Company's exposure to "Other" CDS contracts is also highly diversified. It includes $1.7 billion of exposure to three pooled infrastructure transactions comprising diversified pools of international infrastructure project transactions and loans to regulated utilities. These pools were all structured with underlying credit enhancement sufficient for the Company to attach at super senior AAA levels at origination. The remaining $2.0 billion of exposure in "Other" CDS contracts comprises numerous deals across various asset classes, such as commercial receivables, international RMBS, infrastructure, regulated utilities and consumer receivables. Of the total net par outstanding in the "Other" sector, $298 million is rated BIG.

Distribution of Credit Derivative Net Par Outstanding by Internal Rating

Ratings	As of March 31, 2013 Net Par Outstanding	As of March 31, 2013 % of Total	As of December 31, 2012 Net Par Outstanding	As of December 31, 2012 % of Total
	(dollars in millions)			
Super Senior	$ 6,163	23.2%	$ 6,627	23.3%
AAA	10,334	38.9	11,363	40.0
AA	1,911	7.2	1,392	4.9
A	1,312	4.9	2,108	7.4
BBB	2,190	8.3	2,176	7.7
BIG	4,635	17.5	4,743	16.7
Total credit derivative net par outstanding	$ 26,545	100.0%	$ 28,409	100.0%

Credit Derivative
U.S. Residential Mortgage-Backed Securities

Vintage	As of March 31, 2013 Net Par Outstanding (in millions)	Original Subordination(1)	Current Subordination(1)	Weighted Average Credit Rating	Net Change in Unrealized Gain (Loss) First Quarter 2013
					(in millions)
2004 and Prior	$ 86	5.8%	17.0%	A-	$ (1)
2005	1,759	31.4	67.3	AA+	4
2006	973	29.4	34.2	A	(54)
2007	2,550	18.4	8.1	B	(313)
Total	$ 5,368	24.2%	30.2%	BBB	$ (364)

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

Net Change in Fair Value of Credit Derivatives

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

	First Quarter 2013	First Quarter 2012
	(in millions)	
Net credit derivative premiums received and receivable	$ 11	$ 15
Net ceding commissions (paid and payable) received and receivable	1	1
Realized gains on credit derivatives	12	16
Net credit derivative losses (paid and payable) recovered and recoverable	(15)	(68)
Total realized gains (losses) and other settlements on credit derivatives	(3)	(52)
Net unrealized gains (losses) on credit derivatives	(431)	(473)
Net change in fair value of credit derivatives	$ (434)	$ (525)

In First Quarter 2012, CDS contracts totaling $89 million in net par were terminated resulting in accelerations of credit derivative revenue of $0.1 million in First Quarter 2012. There were no terminations in First Quarter 2013.

Changes in the fair value of credit derivatives occur primarily because of changes in interest rates, credit spreads, notional amounts, credit ratings of the referenced entities, expected terms, realized gains (losses) and other settlements, and the issuing company's own credit rating, credit spreads and other market factors. Except for net estimated credit impairments (i.e., net expected loss to be paid as discussed in Note 5), the unrealized gains and losses on credit derivatives are expected to reduce to zero as the exposure approaches its maturity date. With considerable volatility continuing in the market, unrealized gains (losses) on credit derivatives may fluctuate significantly in future periods.

Net Change in Unrealized Gains (Losses) on Credit Derivatives By Sector

	First Quarter	
Asset Type	**2013**	**2012**
	(in millions)	
Pooled corporate obligations:		
CLOs/Collateralized bond obligations	$ (20)	$ 5
Synthetic investment grade pooled corporate	0	—
TruPS CDOs	(32)	(10)
Market value CDOs of corporate obligations	(10)	0
Total pooled corporate obligations	(62)	(5)
U.S. RMBS:		
Option ARM and Alt-A first lien	(224)	(405)
Subprime first lien	(71)	(74)
Prime first lien	(71)	(31)
CES and HELOC	2	—
Total U.S. RMBS	(364)	(510)
CMBS	(3)	0
Other	(2)	42
Total	$ (431)	$ (473)

During First Quarter 2013, unrealized fair value losses were generated primarily in the U.S. RMBS sectors, as well as pooled corporate obligations, due to wider implied net spreads. The wider implied net spreads were primarily a result of the decreased cost to buy protection in AGC's name as the market cost of AGC's credit protection decreased significantly during the period. These transactions were pricing at or above their floor levels (or the minimum rate at which the Company would consider assuming these risks based on historical experience); therefore when the cost of purchasing CDS protection on AGC, which management refers to as the CDS spread on AGC, decreased the implied spreads that the Company would expect to receive on these transactions increased. As indicated below, the credit spreads of both the 5 Year and 1 Year CDS spread on AGC decreased significantly in First Quarter 2013. To calculate the fair value of the Company's CDS contracts, the Company matches the tenor of the CDS contracts in the Company's portfolio to the tenor of the CDS spread purchased in AGC's name.

During First Quarter 2012, unrealized fair value losses were generated primarily in U.S. RMBS sectors primarily as a result of the decreased cost to buy protection in AGC's name as the market cost of AGC's credit protection decreased. These transactions were pricing above their floor levels; therefore when the cost of purchasing CDS protection on AGC decreased the implied spreads that the Company would expect to receive on these transactions increased.

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

Five-Year CDS Spread on AGC

	As of March 31, 2013	As of December 31, 2012	As of December 31, 2011
Quoted price of CDS contract (in basis points):	397	678	1,140

One-Year CDS Spread on AGC

	As of March 31, 2013	As of December 31, 2012	As of December 31, 2011
Quoted price of CDS contract (in basis points):	59	270	965

Components of Credit Derivative Assets (Liabilities)

	As of March 31, 2013	As of December 31, 2012
	(in millions)	
Credit derivative assets	$ 471	$ 388
Credit derivative liabilities	(2,033)	(1,512)
Net fair value of credit derivatives	$ (1,562)	$ (1,124)

	As of March 31, 2013	As of December 31, 2012
	(in millions)	
Fair value of credit derivatives before effect of AGC credit spread	$ (2,808)	$ (3,129)
Plus: Effect of AGC credit spread	1,246	2,005
Net fair value of credit derivatives	$ (1,562)	$ (1,124)

The fair value of CDS contracts at March 31, 2013 before considering the implications of AGC's credit spreads, is a direct result of continued wide credit spreads in the fixed income security markets, and ratings downgrades. The asset classes that remain most affected are 2005-2007 vintages of prime first lien, Alt-A, Option ARM, subprime RMBS deals as well as trust-preferred and pooled corporate securities. Comparing March 31, 2013 with December 31, 2012, there was a narrowing of spreads primarily related to Option ARM and Alt-A first lien, and subprime RMBS transactions. This narrowing of spreads resulted in a gain of approximately $321 million before taking into account AGC's credit spreads.

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

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

Net Fair Value and Expected Losses of Credit Derivatives by Sector

Asset Type	Fair Value of Credit Derivative Asset (Liability), net		Present Value of Expected Claim (Payments) Recoveries (1)	
	As of March 31, 2013	As of December 31, 2012	As of March 31, 2013	As of December 31, 2012
	(in millions)			
Pooled corporate obligations:				
CLOs/Collateralized bond obligations	$ (14)	$ 7	$ —	$ —
Synthetic investment grade pooled corporate	1	1	—	—
TruPS CDOs	(24)	8	(10)	(12)
Market value CDOs of corporate obligations	(8)	1	—	—
Total pooled corporate obligations	(45)	17	(10)	(12)
U.S. RMBS:				
Option ARM and Alt-A first lien	(1,075)	(829)	(91)	(102)
Subprime first lien	(93)	(44)	(65)	(58)
Prime first lien	(153)	(84)	(5)	—
Total U.S. RMBS	(1,321)	(957)	(161)	(160)
CMBS	(4)	(1)	—	—
Other	(192)	(183)	(73)	(67)
Total	$ (1,562)	$ (1,124)	$ (244)	$ (239)

(1) Represents amount in excess of the present value of future installment fees to be received of $31 million as of March 31, 2013 and $33 million as of December 31, 2012. Includes R&W benefit of $172 million as of March 31, 2013 and $181 million as of December 31, 2012.

Ratings Sensitivities of Credit Derivative Contracts

Within the Company's insured CDS portfolio, the transaction documentation for approximately $2.0 billion in CDS gross par insured as of March 31, 2013, provides that a downgrade of AGC's financial strength rating below BBB- or Baa3 would constitute a termination event that would allow the relevant CDS counterparty to terminate the affected transactions. If the CDS counterparty elected to terminate the affected transactions, AGFP, the affiliate of AGC that enters into the credit derivative transactions as the seller of protection, as to which AGC is the credit support provider, could be required to make a termination payment (or may be entitled to receive a termination payment from the CDS counterparty). Of the transactions described above, for one of the CDS counterparties, a downgrade of AGC's financial strength rating below A- or A3 (but not below BBB- or Baa3) would constitute a termination event for which AGC has the right to cure by posting collateral, assigning its rights and obligations in respect of the transactions to a third party, or seeking a third party guaranty of its obligations. No counterparty had a right to terminate any transactions as a result of the January 2013 Moody's downgrade of AGC. AGC does not believe that it can accurately estimate the termination payments that could be required to be made if, as a result of any such downgrade, a CDS counterparty terminated the affected transactions. These payments could have a material adverse effect on the Company's liquidity and financial condition.

The transaction documentation for approximately $12.3 billion in CDS gross par insured as of March 31, 2013, requires certain of the Company's insurance subsidiaries to post eligible collateral to secure its obligation to make payments under such contracts based on (i) the mark-to-market valuation of the underlying exposure and (ii) in some cases, the financial strength ratings of such subsidiaries. Eligible collateral is generally cash or U.S. government or agency securities; eligible collateral other than cash is valued at a discount to the face amount.

- For approximately $11.9 billion of such contracts, AGC has negotiated caps such that, after giving effect to the January 2013 Moody's downgrade of AGC, the posting requirement cannot exceed a certain fixed amount, regardless of the mark-to-market valuation of the exposure or the financial strength ratings of AGC. For such contracts, AGC need not post on a cash basis more than $675 million, which amount is already being posted by AGC and is part of the approximately $708 million AGC is posting.

- For the remaining approximately $400 million of such contracts, AGC could be required from time to time to post additional collateral based on movements in the mark-to-market valuation of the underlying exposure. Of the $708 million AGC is posting, approximately $64 million relate to such $400 million of notional.

Sensitivity to Changes in Credit Spread

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

Effect of Changes in Credit Spread
As of March 31, 2013

Credit Spreads(1)	Estimated Net Fair Value (Pre-Tax)	Estimated Change in Gain/(Loss) (Pre-Tax)
	(in millions)	
100% widening in spreads	$ (3,192)	$ (1,630)
50% widening in spreads	(2,377)	(815)
25% widening in spreads	(1,969)	(407)
10% widening in spreads	(1,724)	(162)
Base Scenario	(1,562)	—
10% narrowing in spreads	(1,406)	156
25% narrowing in spreads	(1,178)	384
50% narrowing in spreads	(799)	763

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

9. Consolidation of Variable Interest Entities

The Company provides financial guaranties with respect to debt obligations of special purpose entities, including VIEs. AGC does not sponsor any VIEs when underwriting third party financial guaranty insurance or credit derivative transactions, nor does it act as the servicer or collateral manager for any VIE obligations that it insures. The transaction structure generally provides certain financial protections to the Company. This financial protection can take several forms, the most common of which are overcollateralization, first loss protection (or subordination) and excess spread. In the case of overcollateralization (i.e., the principal amount of the securitized assets exceeds the principal amount of the structured finance obligations guaranteed by the Company), the structure allows defaults of the securitized assets before a default is experienced on the structured finance obligation guaranteed by the Company. In the case of first loss, the financial guaranty insurance policy only covers a senior layer of losses experienced by multiple obligations issued by special purpose entities, including VIEs. The first loss exposure with respect to the assets is either retained by the seller or sold off in the form of equity or mezzanine debt to other investors. In the case of excess spread, the financial assets contributed to special purpose entities, including VIEs, generate cash flows that are in excess of the interest payments on the debt issued by the special purpose entity. Such excess spread is typically distributed through the transaction's cash flow waterfall and may be used to create additional credit enhancement, applied to redeem debt issued by the special purpose entities, including VIEs (thereby, creating additional overcollateralization), or distributed to equity or other investors in the transaction.

AGC is not primarily liable for the debt obligations issued by the VIEs they insure and would only be required to make payments on these debt obligations in the event that the issuer of such debt obligations defaults on any principal or interest due. AGC's creditors do not have any rights with regard to the collateral supporting the debt issued by FG VIEs. Proceeds from sales, maturities, prepayments and interest from such underlying collateral may only be used to pay Debt Service on VIE liabilities. Net fair value gains and losses on FG VIEs are expected to reverse to zero at maturity of the VIE debt, except for net premiums received and receivable and claims paid and expected to be paid by AGC under the financial guaranty insurance contract. The Company's estimate of expected loss to be paid for FG VIEs is included in Note 5, Expected Loss to be Paid.

As part of the terms of its financial guaranty contracts, the Company obtains certain protective rights with respect to the VIE that are triggered by the occurrence of certain events, such as failure to be in compliance with a covenant due to poor deal performance or a deterioration in a servicer or collateral manager's financial condition. At deal inception, the Company typically is not deemed to control a VIE; however, once a trigger event occurs, the Company's control of the VIE typically increases. The Company continuously evaluates its power to direct the activities that most significantly impact the economic performance of VIEs that have debt obligations insured by the Company and, accordingly, where the Company is obligated to absorb VIE losses or receive benefits that could potentially be significant to the VIE. The Company obtains protective rights under its insurance contracts that give the Company additional controls over a VIE if there is either deterioration of deal performance or in the financial health of the deal servicer. The Company is deemed to be the control party under GAAP, typically when its protective rights give it the power to both terminate and replace the deal servicer, which are characteristics specific to the Company's financial guaranty contracts. If the Company's protective rights that could make it the control party have not been triggered, then it does not consolidate the VIE. As of March 31, 2013, the Company had issued financial guaranty contracts for approximately 600 VIEs that it did not consolidate.

Consolidated FG VIEs

Number of FG VIE's Consolidated

	As of March 31, 2013	As of December 31, 2012
Beginning of the period	8	7
Consolidated(1)	—	1
End of the period	8	8

(1) Net loss on consolidation was $1 million in 2012 and was recorded in “fair value gains (losses) on FG VIEs” in the consolidated statement of operations.

The total unpaid principal balance for the FG VIEs’ assets that were over 90 days or more past due was approximately $227 million. The aggregate unpaid principal of the FG VIEs’ assets was approximately $563 million greater than the aggregate fair value at March 31, 2013. The change in the instrument-specific credit risk of the FG VIEs’ assets for First Quarter 2013 were gains of $20 million.

The aggregate unpaid principal balance was approximately $501 million greater than the aggregate fair value of the FG VIEs’ liabilities as of March 31, 2013.

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

Consolidated FG VIEs
By Type of Collateral

	As of March 31, 2013			As of December 31, 2012		
	Number of FG VIEs	Assets	Liabilities	Number of FG VIEs	Assets	Liabilities
		(dollars in millions)				
With recourse:						
Alt-A first lien	1	$ 47	$ 51	1	$ 47	$ 49
Subprime	1	7	7	1	7	8
Closed-end second lien	5	76	112	5	79	116
Life insurance	1	336	336	1	311	311
Total with recourse	8	466	506	8	444	484
Without recourse	—	399	399	—	374	374
Total	8	$ 865	$ 905	8	$ 818	$ 858

Unpaid Principal for FG VIEs' Liabilities with Recourse

	As of March 31, 2013	As of December 31, 2012
	(in millions)	
Unpaid principal for FG VIEs' liabilities with recourse	$ 711	$ 721

Contractual maturities of FG VIE liabilities with recourse are due in 2027, 2033, 2037 and 2038 for the amounts of $33 million, $10 million, $628 million, and $40 million, respectively.

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

Effect of Consolidating FG VIEs on Net Income and Shareholder's Equity

	First Quarter	
	2013	2012
	(in millions)	
Net earned premiums	$ 0	$ (1)
Net investment income	0	(1)
Net realized investment gains (losses)	0	—
Fair value gains (losses) on FG VIEs	(5)	(6)
Loss and LAE	(1)	(3)
Total pretax effect on net income	(6)	(11)
Less: tax provision (benefit)	(2)	(4)
Total effect on net income (loss)	$ (4)	$ (7)

	As of March 31, 2013	As of December 31, 2012
	(in millions)	
Total (decrease) increase on shareholder's equity	$ (29)	$ (26)

Fair value gains (losses) on FG VIEs represent the net change in fair value on the consolidated FG VIEs' assets and liabilities. For First Quarter 2013, the Company recorded a pre-tax fair value loss on FG VIEs of $5 million.The Company saw price appreciation across all of the Company's FG VIE assets and liabilities as a result of the overall financial market continuing to improve in First Quarter 2013. The most significant price appreciation occurred in first and second lien transactions where the price appreciation was slightly greater on the FG VIE liabilities than on the FG VIE assets. This was a result of market participants giving more value to the guarantees provided by monoline insurers.

During First Quarter 2012, the Company saw price appreciation across all of the Company's FG VIE assets and liabilities as a result of positive economic data at the beginning of the year. However, the price appreciation was greater on the wrapped FG VIEs liabilities during the period, as market participants gave more value to the guarantees provided by monoline insurers. This resulted in a pre-tax fair value loss on FG VIEs of $6 million during the period.

Non-Consolidated VIEs

To date, the Company's analyses have indicated that it does not have a controlling financial interest in any other VIEs and, as a result, they are not consolidated in the consolidated financial statements. The Company's exposure provided through

its financial guaranties with respect to debt obligations of special purpose entities is included within net par outstanding in Note 3, Outstanding Exposure.

10. Investments and Cash

Investment Portfolio

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. Income earned on the general portfolio excluding loss mitigation bonds declined due to lower reinvestment rates. Accrued investment income on fixed maturity securities and short-term investments was $29 million and $30 million as of March 31, 2013 and December 31, 2012, respectively.

Net Investment Income

	First Quarter	
	2013	2012
	(in millions)	
Income from fixed maturity securities in general investment portfolio	$ 20	$ 23
Income from fixed maturity securities purchased or obtained for loss mitigation purposes	2	2
Income from short-term investments	0	0
Gross investment income	22	25
Investment expenses	0	0
Net investment income	$ 22	$ 25

Net Realized Investment Gains (Losses)

	First Quarter	
	2013	2012
	(in millions)	
Realized gains on investment portfolio	$ 22	$ 1
Realized losses on investment portfolio	0	0
Other-than-temporary impairment ("OTTI") (1)	(2)	(2)
Net realized investment gains (losses)	$ 20	$ (1)

(1) Substantially all amounts relate to the credit component of OTTI securities as opposed to OTTI due to intent to sell.

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

Roll Forward of Credit Losses in the Investment Portfolio

	First Quarter	
	2013	2012
	(in millions)	
Balance, beginning of period	$ 15	$ 4
Additions for credit losses on securities for which an OTTI was not previously recognized	—	2
Additions for credit losses on securities for which an OTTI was previously recognized	2	0
Balance, end of period	$ 17	$ 6

Fixed Maturity Securities and Short Term Investments
by Security Type
As of March 31, 2013

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI(2) Gain (Loss) on Securities with OTTI	Weighted Average Credit Quality(3)
			(dollars in millions)				
Fixed maturity securities:							
U.S. government and agencies	17%	$ 457	$ 21	$ 0	$ 478	$ —	AA+
Obligations of state and political subdivisions	63	1,696	144	(11)	1,829	2	AA
Corporate securities	5	128	12	0	140	—	A+
Mortgage-backed securities(4):							
RMBS	3	84	6	(21)	69	(19)	BBB
CMBS	3	68	6	0	74	—	AA+
Asset-backed securities	1	28	2	(2)	28	2	BIG
Foreign government securities	3	76	8	0	84	—	AA+
Total fixed maturity securities	95	2,537	199	(34)	2,702	(15)	AA
Short-term investments	5	144	0	0	144	—	AAA
Total investment portfolio	100%	$ 2,681	$ 199	$ (34)	$ 2,846	$ (15)	AA

Fixed Maturity Securities and Short Term Investments
by Security Type
As of December 31, 2012

Investment Category	Percent of Total(1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI Gain (Loss) on Securities with OTTI	Weighted Average Credit Quality(3)
			(dollars in millions)				
Fixed maturity securities:							
U.S. government and agencies	15%	$ 404	$ 22	$ 0	$ 426	$ —	AA+
Obligations of state and political subdivisions	64	1,713	158	(11)	1,860	2	AA
Corporate securities	5	123	13	0	136	—	A+
Mortgage-backed securities(4):							
RMBS	4	118	6	(23)	101	(21)	A-
CMBS	3	74	8	0	82	—	AAA
Asset-backed securities	1	28	1	(3)	26	1	BIG
Foreign government securities	3	83	9	0	92	—	AAA
Total fixed maturity securities	95	2,543	217	(37)	2,723	(18)	AA
Short-term investments	5	130	0	0	130	—	AAA
Total investment portfolio	100%	$ 2,673	$ 217	$ (37)	$ 2,853	$ (18)	AA

(1) Based on amortized cost.

(2) Accumulated Other Comprehensive Income ("AOCI"). See also Note 16.

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

(4) Government agency obligations were approximately 30% of mortgage backed securities as of March 31, 2013 and 41% as of December 31, 2012 based on fair value.

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

The following tables present the fair value of the Company's available-for-sale municipal bond portfolio as of March 31, 2013 and December 31, 2012 by state, excluding $122 million and $141 million of pre-refunded bonds, respectively. The credit ratings are based on the underlying ratings and do not include any benefit from bond insurance.

Fair Value of Available-for-Sale Municipal Bond Portfolio by State
As of March 31, 2013

State	State General Obligation	Local General Obligation	Revenue	Fair Value	Amortized Cost	Average Credit Rating
			(in millions)			
Texas	$ 33	$ 124	$ 131	$ 288	$ 263	AA
New York	—	35	178	213	196	AA
California	—	43	151	194	190	A
Florida	13	14	76	103	94	AA-
Massachusetts	22	13	67	102	92	AA
Illinois	—	18	52	70	66	AA-
Arizona	—	—	65	65	60	AA
Washington	22	—	42	64	59	AA
Georgia	—	8	55	63	60	AA
Ohio	—	18	27	45	41	AA-
All others	112	74	314	500	465	AA
Total	$ 202	$ 347	$ 1,158	$ 1,707	$ 1,586	AA

Fair Value of Available-for-Sale Municipal Bond Portfolio by State
As of December 31, 2012

State	State General Obligation	Local General Obligation	Revenue	Fair Value	Amortized Cost	Average Credit Rating
			(in millions)			
Texas	$ 33	$ 126	$ 132	$ 291	$ 263	AA
New York	—	36	180	216	196	AA
California	—	44	152	196	190	A+
Massachusetts	22	13	68	103	93	AA
Florida	13	14	75	102	93	AA-
Illinois	—	19	50	69	65	AA-
Washington	23	—	42	65	60	AA
Arizona	—	—	64	64	58	AA
Georgia	—	8	51	59	56	AA
Hawaii	21	7	18	46	42	AA
All others	95	86	327	508	469	AA
Total	$ 207	$ 353	$ 1,159	$ 1,719	$ 1,585	AA

The revenue bond portfolio is comprised primarily of essential service revenue bonds issued by water and sewer authorities and other utilities, transportation authorities, universities and healthcare providers.

Revenue Sources

Type	As of March 31, 2013		As of December 31, 2012	
	Fair Value	Amortized Cost	Fair Value	Amortized Cost
	(in millions)			
Water and sewer	$ 248	$ 229	$ 245	$ 224
Tax backed	245	224	248	225
Transportation	214	197	214	196
Municipal utilities	159	147	162	149
Higher education	152	140	155	141
All others	140	146	135	141
Total	$ 1,158	$ 1,083	$ 1,159	$ 1,076

The Company's investment portfolio is managed by four outside managers. As municipal investments are a material portion of the Company's overall investment portfolio, the Company has established detailed guidelines regarding credit quality, exposure to a particular sector and exposure to a particular obligor within a sector. Each of the portfolio managers perform independent analysis on every municipal security they purchase for the Company's portfolio. The Company meets with each of its portfolio managers quarterly and reviews all investments with a change in credit rating as well as any investments on the manager's watch list of securities with the potential for downgrade.

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

Fixed Maturity Securities
Gross Unrealized Loss by Length of Time
As of March 31, 2013

	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
	(dollars in millions)					
U.S. government and agencies	$ 1	$ 0	$ —	$ —	$ 1	0
Obligations of state and political subdivisions	65	(11)	—	—	65	(11)
Corporate securities	3	0	—	—	3	0
Mortgage-backed securities:						
RMBS	8	0	11	(21)	19	(21)
CMBS	1	0	—	—	1	0
Asset-backed securities	—	—	10	(2)	10	(2)
Foreign government securities	1	0	—	—	1	0
Total	$ 79	$ (11)	$ 21	$ (23)	$ 100	$ (34)
Number of securities		23		2		25
Number of securities with OTTI		—		1		1

Fixed Maturity Securities
Gross Unrealized Loss by Length of Time
As of December 31, 2012

	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
	(dollars in millions)					
U.S. government and agencies	$ 1	$ 0	$ —	$ —	$ 1	$ 0
Obligations of state and political subdivisions	29	(11)	—	—	29	(11)
Corporate securities	2	0	—	—	2	0
Mortgage-backed securities:						
RMBS	3	(1)	12	(22)	15	(23)
CMBS	1	0	—	—	1	0
Asset-backed securities	—	—	9	(3)	9	(3)
Foreign government securities	2	0	—	—	2	0
Total	$ 38	$ (12)	$ 21	$ (25)	$ 59	$ (37)
Number of securities		13		3		16
Number of securities with OTTI		—		2		2

Of the securities in an unrealized loss position for 12 months or more as of March 31, 2013, two securities had unrealized losses greater than 10% of book value. The total unrealized loss for these securities as of March 31, 2013 was $23 million. The Company has determined that the unrealized losses recorded as of March 31, 2013 are yield related and not the result of other-than-temporary impairments.

The amortized cost and estimated fair value of available-for-sale fixed maturity securities by contractual maturity as of March 31, 2013 are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Distribution of Fixed-Maturity Securities
by Contractual Maturity
As of March 31, 2013

	Amortized Cost	Estimated Fair Value
	(in millions)	
Due within one year	$ 21	$ 21
Due after one year through five years	643	672
Due after five years through 10 years	430	476
Due after 10 years	1,291	1,390
Mortgage-backed securities:		
RMBS	84	69
CMBS	68	74
Total	$ 2,537	$ 2,702

To fulfill state licensing requirements the Company has placed on deposit eligible securities of $9 million as of March 31, 2013 and December 31, 2012. To provide collateral for a letter of credit, the Company holds a fixed maturity investment in a segregated account equal to 120% of the letter of credit, which amounted to $3.5 million as of March 31, 2013 and December 31, 2012.

Under certain derivative contracts, AGC is required to post eligible securities as collateral. The need to post collateral under these transactions is generally based on fair value assessments in excess of contractual thresholds. The fair value of

AGC's pledged securities totaled $708 million and $659 million as of March 31, 2013 and December 31, 2012, respectively. See Note 8, Financial Guaranty Contracts Accounted for as Credit Derivatives, for the effect of the downgrade on collateral posted.

No material investments of the Company were non-income producing for First Quarter 2013 and 2012, respectively.

Loss Mitigation Assets

One of the Company's strategies for mitigating losses has been to purchase insured securities that have expected losses at discounted prices. The Company may also obtain the obligations referenced in CDS transactions that have triggered the insured's obligation to put these bonds to AGC.

Loss Mitigation Assets
Carrying Value

	As of March 31, 2013	As of December 31, 2012
	(in millions)	
Fixed maturity securities:		
Obligations of state and political subdivisions	$ 24	$ 23
RMBS	32	34
Asset-backed securities	28	26
Other invested assets	24	41
Total	$ 108	$ 124

11. Insurance Company Regulatory Requirements

Dividend Restrictions and Capital Requirements

AGC is a Maryland domiciled insurance company. As of March 31, 2013, the amount available for distribution from AGC during 2013 with notice to, but without prior approval of, the Maryland Commissioner of Insurance under the Maryland insurance law is approximately $91 million.

Dividends Paid

	First Quarter	
	2013	2012
	(in millions)	
Dividends paid by AGC to Assured Guaranty US Holdings Inc.	$ —	$ 15

12. Income Taxes

Provision for Income Taxes

AGC and AGUK are subject to U.S. and United Kingdom income tax, respectively. AGC and AGUK are subject to income taxes imposed by U.S. and United Kingdom authorities at marginal corporate income tax rates of 35% and 23.25%, respectively, and file applicable tax returns. For periods subsequent to April 1, 2013, the U.K. corporation tax rate has been reduced to 23%, for the period April 1, 2012 to April 1, 2013 the U.K. corporation tax rate was 24% resulting in a blended tax rate of 23.25% in 2013 and prior to April 1, 2012, the U.K. corporation rate was 26% resulting in a blended tax rate of 24.5% in 2012. The Company's overall corporate effective tax rate fluctuates based on the distribution of income across jurisdictions.

The Company's provision for income taxes for interim financial periods is not based on an estimated annual effective rate due to the variability in fair value of its credit derivatives, which prevents the Company from projecting a reliable estimated annual effective tax rate and pretax income for the full year 2013. A discrete calculation of the provision is calculated for each interim period.

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

Effective Tax Rate Reconciliation

	First Quarter	
	2013	2012
	(in millions)	
Expected tax provision (benefit) at statutory rates in taxable jurisdictions	$ (134)	$ (188)
Tax-exempt interest	(4)	(5)
Change in liability for uncertain tax positions	(8)	1
Total provision (benefit) for income taxes	$ (146)	$ (192)
Effective tax rate	38.2%	35.7%

The expected tax provision at statutory rates in taxable jurisdictions is calculated as the sum of pretax income in each jurisdiction multiplied by the statutory tax rate of the jurisdiction by which it will be taxed. Pretax income of the Company's subsidiaries which are not U.S. domiciled but are subject to U.S. tax by election or as controlled foreign corporations are included at the U.S. statutory tax rate.

Valuation Allowance

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

Uncertain Tax Positions

The following table provides a reconciliation of the beginning and ending balances of the total liability for unrecognized tax benefits. The balance of unrecognized tax benefits has been reduced due to the closing of an IRS audit.

	As of March 31, 2013	As of December 31, 2012
	(in millions)	
Balance at the beginning of the period	$ 17	$ 15
Decrease due to closing of IRS audit	(9)	—
Increase in unrecognized tax benefits as a result of position taken during the current period	1	2
Balance, end of period	9	$ 17

The Company's policy is to recognize interest and penalties related to uncertain tax positions in income tax expense. As of March 31, 2013, the Company has accrued $1 million of interest.

In the consolidated balance sheet as of December 31, 2012, current income tax payable of $36 million was reclassified to other liabilities to conform to the current year's presentation.

13. Reinsurance and Other Monoline Exposures

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

Assumed and Ceded Business

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

- if the Company fails to meet certain financial and regulatory criteria and to maintain a specified minimum financial strength rating or
- upon certain changes of control of the Company.

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

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

With respect to a significant portion of the Company's in-force financial guaranty Assumed Business, based on AGC's current ratings and subject to the terms of each reinsurance agreement, the ceding company may have the right to recapture Assumed Business ceded to AGC and in most cases, assets representing the statutory unearned premium (net of ceding commissions) and loss reserves (if any), plus in certain cases an additional ceding commission, associated with that business.

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

Effect of Reinsurance on Statement of Operations

	First Quarter	
	2013	2012
	(in millions)	
Premiums Written:		
Direct	$ 2	$ 10
Assumed	0	22
Ceded	(4)	(15)
Net	$ (2)	$ 17
Premiums Earned:		
Direct	$ 36	$ 23
Assumed	5	5
Ceded	(20)	(8)
Net	$ 21	$ 20
Loss and LAE:		
Direct	$ (12)	$ (6)
Assumed	(14)	24
Ceded	10	(2)
Net	$ (16)	$ 16

Reinsurer Exposure

In addition to assumed and ceded reinsurance arrangements, the Company may also have exposure to some financial guaranty reinsurers (i.e., monolines) in other areas. Second-to-pay insured par outstanding represents transactions the Company has insured that were previously insured by other monolines. The Company underwrites such transactions based on the underlying insured obligation without regard to the primary insurer. Another area of exposure is in the investment portfolio where the Company holds fixed maturity securities that are wrapped by monolines and whose value may decline based on the rating of the monoline. At March 31, 2013, based on fair value, the Company had $121 million of fixed maturity securities in its investment portfolio wrapped by Ambac Assurance Corporation (“Ambac”), $99 million by National Public Finance Guarantee Corporation, $88 million by AGM and $5 million by other guarantors.

Exposure by Reinsurer

Reinsurer	Ratings as of June 7, 2013		Par Outstanding as of March 31, 2013		
	Moody's Reinsurer Rating	S&P Reinsurer Rating	Ceded Par Outstanding(1)	Second-to-Pay Insured Par Outstanding	Assumed Par Outstanding
			(dollars in millions)		
Affiliated Companies	(2)	(2)	$ 34,779	$ 803	$ —
Non-Affiliated Companies:					
American Overseas Reinsurance Company Limited (f/k/a Ram Re)	WR(3)	WR	2,010	—	—
Radian Asset Assurance Inc.	Ba1	B+	96	1	998
Ambac	WR	WR	85	1,962	1,100
ACA Financial Guaranty Corp.	NR	WR	10	1	1
MBIA Inc.	(4)	(4)	—	1,437	3,315
CIFG Assurance North America Inc. ("CIFG")	WR	WR	—	109	2,632
Financial Guaranty Insurance Co.	WR	WR	—	1,114	269
Syncora Guarantee Inc.	WR	WR	—	703	15
Other	Various	Various	77	860	—
Non-Affiliated Companies			2,278	6,187	8,330
Total			$ 37,057	$ 6,990	$ 8,330

(1) Includes $9,729 million in ceded par outstanding related to insured credit derivatives.

(2) The affiliates of AGC are Assured Guaranty Re Ltd. and its subsidiaries ("AG Re") rated Baa1 by Moody's and AA- by S&P and AGM and its subsidiaries rated A2 by Moody's and AA- by S&P.

(3) Represents "Withdrawn Rating."

(4) MBIA Inc. includes various subsidiaries which are rated A and B by S&P and Baa1, B1, B3, WR and NR by Moody's.

Amounts Due (To) From Reinsurers
As of March 31, 2013

	Assumed Premium, net of Commissions	Ceded Premium, net of Commissions	Assumed Expected Loss and LAE	Ceded Expected Loss and LAE
		(in millions)		
Affiliated Companies	$ —	$ (79)	$ —	$ 186
American Overseas Reinsurance Company Ltd. (f/k/a Ram Re)	—	(2)	—	3
Ambac	4	—	(8)	—
MBIA Inc.	0	—	(15)	—
Financial Guaranty Insurance Co.	0	—	(22)	—
Syncora Guarantee Inc.	—	—	19	—
Other	—	(2)	—	—
Total	$ 4	$ (83)	$ (26)	$ 189

14. Commitments and Contingencies

Legal Proceedings

Litigation

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

In addition, in the ordinary course of its business, AGC and AGUK assert claims in legal proceedings against third parties to recover losses paid in prior periods. For example, as described in Note 5, Expected Loss to be Paid "Recovery Litigation", as of the date of this filing, AGC has filed complaints against certain sponsors and underwriters of RMBS securities that AGC had insured, alleging, among other claims, that such persons had breached R&W in the transaction documents, failed to cure or repurchase defective loans and/or violated state securities laws. The amounts, if any, the Company will recover in proceedings to recover losses are uncertain, and recoveries, or failure to obtain recoveries, in any one or more of these proceedings during any quarter or year could be material to the Company's results of operations in that particular quarter or year.

Proceedings Relating to the Company's Financial Guaranty Business

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

Beginning in July 2008, AGC's affiliate AGM and various other financial guarantors were named in complaints filed in the Superior Court for the State of California, City and County of San Francisco. Since that time, plaintiffs' counsel has filed amended complaints against AGC and AGM and added additional plaintiffs. As of the date of this filing, the plaintiffs with complaints against AGC and AGM, among other financial guaranty insurers, are: (a) *City of Los Angeles, acting by and through the Department of Water and Power;* (b) *City of Sacramento;* (c) *City of Los Angeles;* (d) *City of Oakland;* (e) *City of Riverside;* (f) *City of Stockton ;* (g) *County of Alameda;* (h) *Contra Costa County;* (i) *County of San Mateo;* (j) *Los Angeles World Airports;* (k) *City of Richmond;* (l) *Redwood City;* (m) *East Bay Municipal Utility District;* (n) *Sacramento Suburban Water District;* (o) *City of San Jose;* (p) *County of Tulare;* (q) *The Regents of the University of California;* (r) *The Redevelopment Agency of the City of Riverside;* (s) *The Public Financing Authority of the City of Riverside;* (t) *The Jewish Community Center of San Francisco;* (u) *The San Jose Redevelopment Agency;* (v) *The Redevelopment Agency of the City of Stockton;* (w) *The Public Financing Authority of the City of Stockton; and* (x) *The Olympic Club*. Complaints filed by the City and County of San Francisco and the Sacramento Municipal Utility District were subsequently dismissed against AGC and AGM. These complaints allege that the financial guaranty insurer defendants (i) participated in a conspiracy in violation of California's antitrust laws to maintain a dual credit rating scale that misstated the credit default risk of municipal bond issuers and created market demand for municipal bond insurance, (ii) participated in risky financial transactions in other lines of business that damaged each insurer's financial condition (thereby undermining the value of each of their guaranties), and (iii) failed to adequately disclose the impact of those transactions on their financial condition. In addition to their antitrust claims, various plaintiffs in these actions assert claims for breach of the covenant of good faith and fair dealing, fraud, unjust enrichment, negligence, and negligent misrepresentation. At hearings held in July and October 2011 relating to AGC, AGM and the other defendants' demurrer, the court overruled the demurrer on the following claims: breach of contract, violation of California's antitrust statute and of its unfair business practices law, and fraud. The remaining claims were dismissed. On December 2, 2011, AGM, AGC and the other bond insurer defendants filed an anti-SLAPP ("Strategic Lawsuit Against Public Participation") motion to strike the complaints under California's Code of Civil Procedure. On May 1, 2012, the court ruled in favor of the bond insurer defendants on the first prong of the anti-SLAPP motion as to the causes of action arising from the alleged conspiracy, but denied the motion as to those causes of action based on transaction specific representations and omissions about the bond insurer defendants' credit ratings and financial health. The court held hearings on the second prong of the anti-SLAPP motion on March 21, 2013 and April 22, 2013. At the March 21, 2013 hearing, the court issued an oral ruling that, under the second prong of the anti-SLAPP motion, there has been no showing of an antitrust act claim against the defendants. At the April 22, 2013 hearing, the court issued another oral ruling that, under the second prong of the anti-SLAPP motion, plaintiffs had offered sufficient evidence of a claim under California's Unfair Competition Law and denied defendants' motion to strike. The complaints in these lawsuits generally seek unspecified monetary damages, interest, attorneys' fees, costs and other expenses. The Company cannot reasonably estimate the possible loss or range of loss, if any, that may arise from these lawsuits.

On April 8, 2011, AGC and its affiliate AG Re filed a Petition to Compel Arbitration with the Supreme Court of the State of New York, requesting an order compelling Ambac to arbitrate Ambac's disputes with AGC and AG Re concerning their obligations under reinsurance agreements with Ambac. In March 2010, Ambac placed a number of insurance policies that it had issued, including policies reinsured by AGC and AG Re pursuant to the reinsurance agreements, into a segregated account. The Wisconsin state court has approved a rehabilitation plan whereby permitted claims under the policies in the segregated account will be paid 25% in cash and 75% in surplus notes issued by the segregated account. Ambac has advised AGC and AG Re that it has and intends to continue to enter into commutation agreements with holders of policies issued by Ambac, and reinsured by AGC and AG Re, pursuant to which Ambac will pay a combination of cash and surplus notes to the policyholder. AG Re and AGC have informed Ambac that they believe their only current payment obligation with respect to the commutations arises from the cash payment, and that there is no obligation to pay any amounts in respect of the surplus notes until payments of principal or interest are made on such notes. Ambac has disputed this position on one commutation and may take a similar position on subsequent commutations. On April 15, 2011, attorneys for the Wisconsin Insurance Commissioner, as Rehabilitator of Ambac's segregated account, and for Ambac filed a motion with Lafayette County,Wisconsin, Circuit Court Judge William Johnston, asking him to find AGC and AG Re to be in violation of an injunction protecting the interests of the segregated account by their seeking to compel arbitration on this matter and failing to pay in full all amounts with respect to Ambac's payments in the form of surplus notes. On June 14, 2011, Judge Johnston issued an order granting the Rehabilitator's and Ambac's motion to enforce the injunction against AGC and AG Re and the parties filed a stipulation dismissing the Petition to Compel Arbitration without prejudice. AGC and AG Re have appealed Judge Johnston's order to the Wisconsin Court of Appeals.

On November 28, 2011, Lehman Brothers International (Europe) (in administration) ("LBIE") sued AGFP, an affiliate of AGC which in the past had provided credit protection to counterparties under credit default swaps. AGC acts as the credit support provider of AGFP under these credit default swaps. LBIE's complaint, which was filed in the Supreme Court of the State of New York, alleged that AGFP improperly terminated nine credit derivative transactions between LBIE and AGFP and improperly calculated the termination payment in connection with the termination of 28 other credit derivative transactions between LBIE and AGFP. With respect to the 28 credit derivative transactions, AGFP calculated that LBIE owes AGFP approximately $25 million, whereas LBIE asserted in the complaint that AGFP owes LBIE a termination payment of approximately $1.4 billion. LBIE is seeking unspecified damages. On February 3, 2012, AGFP filed a motion to dismiss certain of the counts in the complaint, and on March 15, 2013, the court granted AGFP's motion to dismiss the count relating to improper termination of the nine credit derivative transactions and denied AGFP's motion to dismiss the count relating to the remaining transactions. The decision is subject to appeal. The Company cannot reasonably estimate the possible loss, if any, that may arise from this lawsuit.

15. Note Payable to Affiliate and Credit Facilities

Note Payable to Affiliate

On December 18, 2009, AGC issued a surplus note with a principal amount of $300 million to AGM. This Note Payable to Affiliate carries a simple interest rate of 5.0% per annum and matures on December 31, 2029. Principal is payable at the option of AGC prior to the final maturity of the note in 2029 and interest is payable on the note annually in arrears as of December 31st of each year, commencing December 31, 2010. Payments of principal and interest are subject to AGC having policyholders' surplus in excess of statutory minimum requirements after such payment and to prior written approval by the Maryland Insurance Administration.

Letters of Credit

AGC entered into a letter of credit agreement in December 2011 with Bank of New York Mellon totaling approximately $2.9 million in connection with a 2008 lease for office space, which space was subsequently sublet. As of March 31, 2013, $2.9 million was outstanding under this letter of credit. This letter of credit expires in November 2013.

Committed Capital Securities

On April 8, 2005, AGC entered into separate agreements (the "Put Agreements") with four custodial trusts (each, a "Custodial Trust") pursuant to which AGC may, at its option, cause each of the Custodial Trusts to purchase up to $50 million of perpetual preferred stock of AGC (the "AGC Preferred Stock"). The custodial trusts were created as a vehicle for providing capital support to AGC by allowing AGC to obtain immediate access to new capital at its sole discretion at any time through the exercise of the put option. If the put options were exercised, AGC would receive $200 million in return for the issuance of its own perpetual preferred stock, the proceeds of which may be used for any purpose, including the payment of claims. The put

options have not been exercised through the date of this filing. Initially, all of AGC CCS were issued to a special purpose pass-through trust (the "Pass-Through Trust"). The Pass-Through Trust was dissolved in April 2008 and the AGC CCS were distributed to the holders of the Pass-Through Trust's securities. Neither the Pass-Through Trust nor the custodial trusts are consolidated in the Company's financial statements.

Income distributions on the Pass-Through Trust Securities and AGC CCS were equal to an annualized rate of one-month LIBOR plus 110 basis points for all periods ending on or prior to April 8, 2008. Following dissolution of the Pass-Through Trust, distributions on the AGC CCS Securities are determined pursuant to an auction process. On April 7, 2008 this auction process failed, thereby increasing the annualized rate on the AGC CCS to one-month LIBOR plus 250 basis points. Distributions on the AGC preferred stock will be determined pursuant to the same process.

16. Other Comprehensive Income

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

Changes in Accumulated Other Comprehensive Income by Component
First Quarter 2013

	Net Unrealized Gains (Losses) on Investments with no OTTI	Net Unrealized Gains (Losses) on Investments with OTTI	Cumulative Translation Adjustment	Total Accumulated Other Comprehensive Income
	(in millions)			
Balance, December 31, 2012	$ 128	$ (12)	$ (5)	$ 111
Other comprehensive income before reclassifications	(8)	1	(6)	(13)
Amounts reclassified from AOCI to:				
Other net realized investment gains (losses)	(3)	2	—	(1)
Tax (provision) benefit	1	(1)	—	0
Total amounts reclassified from AOCI, net of tax	(2)	1	—	(1)
Net current period other comprehensive income (loss)	(10)	2	(6)	(14)
Balance, March 31, 2013	$ 118	$ (10)	$ (11)	$ 97

First Quarter 2012

	Net Unrealized Gains (Losses) on Investments with no OTTI	Net Unrealized Gains (Losses) on Investments with OTTI	Cumulative Translation Adjustment	Total Accumulated Other Comprehensive Income
	(in millions)			
Balance, December 31, 2011	$ 80	$ 2	$ (8)	$ 74
Other comprehensive income (loss)	23	(16)	1	8
Balance, March 31, 2012	$ 103	$ (14)	$ (7)	$ 82

17. Subsequent Event

Subsequent events have been considered through June 11, 2013, the date on which these financial statements were issued.