

# **Assured Guaranty Re Overseas Ltd.**

**(a wholly-owned subsidiary of Assured Guaranty Re Ltd.)**

## **Consolidated Financial Statements**

**December 31, 2019 and 2018**

**Assured Guaranty Re Overseas Ltd.**

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**December 31, 2019 and 2018**

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## **Report of Independent Auditors**

To the Board of Directors of Assured Guaranty Re Overseas Ltd.

We have audited the accompanying consolidated financial statements of Assured Guaranty Re Overseas Ltd. and its subsidiary (the “Company”), which comprise the consolidated balance sheets as of December 31, 2019 and 2018, and the related consolidated statements of operations, of comprehensive income (loss), of shareholder’s equity and of cash flows for the years then ended.

### ***Management's Responsibility for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Assured Guaranty Re Overseas Ltd. and its subsidiary as of December 31, 2019 and 2018, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

/s/ PricewaterhouseCoopers LLP

New York, New York  
April 15, 2020

# Assured Guaranty Re Overseas Ltd.

## Consolidated Balance Sheets

(dollars in thousands except par value and share amounts)

	As of December 31, 2019	As of December 31, 2018
<b>Assets</b>		
Investment portfolio:		
Fixed-maturity securities, available-for-sale, at fair value (amortized cost of \$358,605 and \$333,716)	\$ 380,503	\$ 337,278
Short-term investments, at fair value	5,809	7,209
Total investment portfolio	386,312	344,487
Loan receivable from affiliate	40,000	50,000
Cash	286	674
Premiums receivable, net of commissions payable	11,236	11,976
Ceded unearned premium reserve	23,375	23,391
Deferred acquisition costs	5,257	5,747
Other assets	3,716	3,554
<b>Total assets</b>	<b>\$ 470,182</b>	<b>\$ 439,829</b>
<b>Liabilities and shareholder's equity</b>		
Unearned premium reserve	\$ 36,530	\$ 35,576
Reinsurance balances payable, net	14,080	15,480
Deferred tax liability, net	5,470	1,599
Other liabilities	4,048	3,822
<b>Total liabilities</b>	<b>60,128</b>	<b>56,477</b>
Commitments and contingencies (see Note 13)		
Common stock (\$1.00 par value, 1,000,000 shares authorized, issued and outstanding in 2019 and 2018)	1,000	1,000
Additional paid-in capital	135,964	135,964
Retained earnings	255,791	243,574
Accumulated other comprehensive income, net of tax of \$4,599 and \$748	17,299	2,814
<b>Total shareholder's equity</b>	<b>410,054</b>	<b>383,352</b>
<b>Total liabilities and shareholder's equity</b>	<b>\$ 470,182</b>	<b>\$ 439,829</b>

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

# Assured Guaranty Re Overseas Ltd.

## Consolidated Statements of Operations

(in thousands)

	Year Ended December 31,	
	2019	2018
<b>Revenues</b>		
Net earned premiums	\$ 6,053	\$ 4,886
Net investment income	14,691	14,199
Net realized investment gains (losses)	(230)	(1,044)
Other income (loss)	127	(10)
<b>Total revenues</b>	<b>20,641</b>	<b>18,031</b>
<b>Expenses</b>		
Loss and loss adjustment expenses (benefit)	2	(149)
Amortization of deferred acquisition costs	956	1,187
Employee compensation and benefit expenses	3,810	3,622
Other operating expenses	1,275	1,214
<b>Total expenses</b>	<b>6,043</b>	<b>5,874</b>
<b>Income (loss) before income taxes</b>	<b>14,598</b>	<b>12,157</b>
Provision (benefit) for income taxes		
Current	2,361	1,750
Deferred	20	127
<b>Total provision (benefit) for income taxes</b>	<b>2,381</b>	<b>1,877</b>
<b>Net income (loss)</b>	<b>\$ 12,217</b>	<b>\$ 10,280</b>

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

# Assured Guaranty Re Overseas Ltd.

## Consolidated Statements of Comprehensive Income (Loss)

(in thousands)

	Year Ended December 31,	
	2019	2018
<b>Net income (loss)</b>	<b>\$ 12,217</b>	<b>\$ 10,280</b>
Change in net unrealized gains (losses) on:		
Investments with no other-than-temporary impairment, net of tax provision (benefit) of \$3,668 and \$(1,754)	13,797	(6,597)
Investments with other-than-temporary impairment, net of tax provision (benefit) of \$183 and \$(7)	688	(27)
<b>Other comprehensive income (loss)</b>	<b>14,485</b>	<b>(6,624)</b>
<b>Comprehensive income (loss)</b>	<b>\$ 26,702</b>	<b>\$ 3,656</b>

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

# Assured Guaranty Re Overseas Ltd.

## Consolidated Statements of Shareholder's Equity

Years Ended December 31, 2019 and 2018

(in thousands)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholder's Equity
<b>Balance at December 31, 2017</b>	<b>\$ 1,000</b>	<b>\$ 135,964</b>	<b>\$ 233,294</b>	<b>\$ 9,438</b>	<b>\$ 379,696</b>
Net income	—	—	10,280	—	10,280
Other comprehensive loss	—	—	—	(6,624)	(6,624)
<b>Balance at December 31, 2018</b>	<b>1,000</b>	<b>135,964</b>	<b>243,574</b>	<b>2,814</b>	<b>383,352</b>
Net income	—	—	12,217	—	12,217
Other comprehensive income	—	—	—	14,485	14,485
<b>Balance at December 31, 2019</b>	<b>\$ 1,000</b>	<b>\$ 135,964</b>	<b>\$ 255,791</b>	<b>\$ 17,299</b>	<b>\$ 410,054</b>

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

# Assured Guaranty Re Overseas Ltd.

## Consolidated Statements of Cash Flows

(in thousands)

	Year Ended December 31,	
	2019	2018
<b>Operating Activities</b>		
Net Income	\$ 12,217	\$ 10,280
Adjustments to reconcile net income to net cash flows provided by operating activities:		
Net amortization of premium (discount) on investments	1,155	1,236
Net realized investment losses (gains)	230	1,044
Change in deferred acquisition costs	490	424
Change in premiums receivable, net of premiums payable and commissions	(658)	(1,860)
Change in ceded unearned premium reserve	16	(1,643)
Change in unearned premium reserve	954	4,021
Other	252	15
<b>Net cash flows provided by (used in) operating activities</b>	<b>\$ 14,656</b>	<b>\$ 13,517</b>
<b>Investing activities</b>		
Fixed-maturity securities:		
Purchases	(62,979)	(88,376)
Sales	28,225	51,238
Maturities	8,454	12,406
Net sales (purchases) of short-term investments with original maturities of less than three months	1,426	(2,833)
Proceeds from repayment of loan to affiliate	10,000	10,000
Other	(170)	—
<b>Net cash flows provided by (used in) investing activities</b>	<b>(15,044)</b>	<b>(17,565)</b>
<b>Net cash flows provided by (used in) financing activities</b>	<b>—</b>	<b>—</b>
Effect of foreign exchange rate changes	—	(3)
<b>Increase (decrease) in cash</b>	<b>(388)</b>	<b>(4,051)</b>
Cash at beginning of period	674	4,725
<b>Cash at end of period</b>	<b>\$ 286</b>	<b>\$ 674</b>
<b>Supplemental cash flow information</b>		
Cash paid (received) during the period for:		
Income taxes	\$ 2,326	\$ 2,124

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



# **Assured Guaranty Re Overseas Ltd.**

## **Notes to Consolidated Financial Statements**

**December 31, 2019 and 2018**

### **1. Business and Basis of Presentation**

#### **Business**

Assured Guaranty Re Overseas Ltd. (AGRO or, together with its subsidiary, the Company) is a wholly-owned subsidiary of Assured Guaranty Overseas US Holdings Inc. (AGOUS), a Delaware corporation, which is a wholly-owned subsidiary of Assured Guaranty Re Ltd. (AG Re), a Bermuda domiciled company. AG Re is a direct subsidiary of Assured Guaranty Ltd. (AGL and, together with its subsidiaries, Assured Guaranty), also a Bermuda domiciled company. AGL provides, through its operating subsidiaries, credit protection products to the United States (U.S.) and international public finance (including infrastructure) and structured finance markets, as well as asset management services.

AGRO was incorporated with limited liability under the Bermuda Companies Act 1981 and is licensed as a Class 3A Insurer and a Class C Long-Term Insurer under the Insurance Act 1978, and amendments thereto and related regulations. AGRO owns AG Intermediary Inc., a New York insurance intermediary company. In 2017, AGRO was granted certified reinsurer status by the Missouri Department of Insurance.

AGRO has provided specialty insurance and reinsurance on various lines of structured finance business that have similar risk profiles to those of the structured finance financial guaranty transactions insured and reinsured by it and its affiliates, as well as reinsurance on structured finance and public finance financial guaranty business. The Company currently provides insurance and reinsurance mainly for life insurance transactions and aircraft residual value insurance (RVI) transactions. Life insurance transactions provide U.S. life insurers and reinsurers capital relief from the excess statutory reserves they are required to hold by U.S. state regulators over what the respective life insurers and reinsurers believe are necessary for level premium term life insurance policies. RVI policies guarantee that a specific, properly maintained asset will have a specified value at a specified future date.

The Company has a portfolio of financial guaranty reinsurance under quota share and excess of loss treaties. Financial guaranty insurance policies provide an unconditional and irrevocable guaranty that protects the holder of a financial obligation against non-payment of scheduled principal and interest (debt service) when due. Upon an obligor's default on scheduled principal or interest payments due on the obligation, the primary insurer is required under the financial guaranty policy to pay the principal or interest shortfall. Under a reinsurance agreement, the reinsurer, in consideration of a premium paid to it, agrees to indemnify another insurer, called the ceding company, for part or all of the liability of the ceding company under one or more insurance policies that the ceding company has issued. While the Company has not provided new financial guaranty reinsurance in the recent past, it may do so again in the future.

#### **Basis of Presentation**

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). In management's opinion, all material adjustments necessary for a fair statement of the financial condition, results of operations and cash flows of the Company are reflected in the periods presented and are of a normal recurring nature. 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.

The consolidated financial statements include the accounts of AGRO and its subsidiary. Intercompany accounts and transactions between and among AGRO and its subsidiary have been eliminated. Certain prior year balances have been reclassified to conform to the current year's presentation.

#### **Significant Accounting Policies**

The Company revalues assets, liabilities, revenue and expenses denominated in non-U.S. currencies into U.S. dollars using applicable exchange rates. Gains and losses relating to translating transactions in foreign denominations are reported in the consolidated statement of operations.

The Company participates in AGL's long term incentive plans. AGL follows the fair value recognition provisions for share based compensation expense. The Company is allocated its proportionate share of expenses, including compensation expense based on time studies conducted annually, in accordance with the Amended and Restated Service Agreement (the Group Service Agreement). See Note 12, Related Party Transactions for additional information.

Other accounting policies are included in the following notes.

### **Accounting Policies**

Premium revenue recognition	Note 4 and Note 7
Loss and loss adjustment expense	Note 5
Policy acquisition costs	Note 6
Fair value measurement	Note 8
Investments and cash	Note 9
Income taxes	Note 10
Loan receivable from affiliate	Note 12
Commitments and contingencies	Note 13

### **Adopted Accounting Standards**

#### ***Premium Amortization on Purchased Callable Debt Securities***

In March 2017, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2017-08, *Receivables-Nonrefundable Fees and Other Costs (Topic 310-20) - Premium Amortization on Purchased Callable Debt Securities*. This ASU shortened the amortization period for the premium on certain purchased callable debt securities to the earliest call date. This ASU was adopted on January 1, 2019, with no effect on the Company's consolidated financial statements.

### **Future Application of Accounting Standards**

#### ***Credit Losses on Financial Instruments***

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The ASU provides a new current expected credit loss model to account for credit losses on certain financial assets (e.g., reinsurance recoverables, premium receivables, and held-to-maturity debt securities) and off-balance sheet exposures. That model requires an entity to estimate lifetime credit losses related to certain financial assets, based on relevant historical information, adjusted for current conditions and reasonable and supportable forecasts that could affect the collectability of the reported amount. The ASU also makes targeted amendments to the current impairment model for available-for-sale debt securities, which includes requiring the recognition of an allowance rather than a direct write-down of the investment, which may be reversed in the event that the credit of an issuer improves. In addition, the ASU eliminates the existing guidance for purchased credit impaired assets and introduces a new model for purchased financial assets with credit deterioration, which requires the recognition of an initial allowance for credit losses. Under the new guidance, the amortized cost will be the purchase price plus the allowance at the acquisition date.

The ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. For reinsurance recoverables, premiums receivable and debt instruments such as loans and held to maturity securities, entities will be required to record a cumulative-effect adjustment to the statement of financial position as of the beginning of the first reporting period in which the guidance is adopted. The changes to the impairment model for available-for-sale securities are to be applied using a modified retrospective approach, and purchased financial assets with credit deterioration are to be applied prospectively. The Company is adopting this ASU, including certain amendments, effective January 1, 2020. ASU 2016-13 will not have a material effect on shareholder's equity at the date of adoption.

## ***Targeted Improvements to the Accounting for Long-Duration Contracts***

In August 2018, the FASB issued ASU 2018-12, *Financial Services - Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts*. The amendments in this ASU:

- improve the timeliness of recognizing changes in the liability for future policy benefits and modify the rate used to discount future cash flows,
- simplify and improve the accounting for certain market-based options or guarantees associated with deposit (or account balance) contracts,
- simplify the amortization of deferred acquisition costs (DAC), and
- improve the effectiveness of the required disclosures.

This ASU does not affect the Company's financial guaranty insurance contracts, but may affect its accounting for certain specialty (non-financial guaranty) contracts. In October 2019, the FASB affirmed its decision to defer the effective date of the ASU to January 1, 2022. The Company does not plan to adopt this ASU until January 1, 2022, and does not expect this ASU to have a material effect on its consolidated financial statements.

## ***Simplification of the Accounting for Income Taxes***

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*. The amendments in this ASU simplify the accounting for income taxes by removing certain exceptions and clarifying certain requirements regarding franchise taxes, goodwill, consolidated tax expenses and annual effective tax rate calculations. The ASU is effective for interim and annual periods beginning after December 15, 2020, with early adoption permitted. The Company is currently assessing the impact of this ASU on its consolidated financial statements.

## **2. Ratings**

The financial strength ratings (or similar rating) for AGRO are AA (stable) as of November 7, 2019 by S&P Global Ratings, a division of Standard & Poor's Financial Services LLC (S&P) and A+ (stable) as of July 12, 2019 by A.M. Best Company, Inc. AGRO's ratings are subject to continuous rating agency review and revision or withdrawal at any time. In addition, the Company periodically assesses the value of each rating assigned to it, and as a result of such assessment may request that a rating agency add or drop a rating.

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

For a discussion of the effects of rating actions on the Company, see Note 7, Reinsurance.

## **3. Outstanding Exposure**

The Company's outstanding exposure is primarily to assumed reinsurance. Approximately 93% and 89% of its gross outstanding exposure was assumed exposure as of December 31, 2019 and December 31, 2018 respectively, with the remainder written on a direct basis. The Company's reinsurance exposure is to both specialty structured finance transactions (life insurance transactions and RVI) and to financial guaranty transactions (both public finance and structured finance).

## **Life Insurance Transactions**

Life insurance transactions assumed by the Company provide U.S. life insurers and reinsurers capital relief from the excess statutory reserves they are required to hold by U.S. state regulators over what the respective life insurers and reinsurers believe are necessary for level premium term life insurance policies. The Company underwrites life insurance transactions by evaluating the amount and type of assets supporting the excess statutory reserves for a pool of life insurance policies. The Company would be required to pay reinsurance claims if mortality rates in the insured pool significantly exceeded currently expected mortality rates and if the assets supporting the excess statutory reserves to cover such an increase in mortality rates were exhausted.

The Company has executed life insurance transactions in both specialty insurance and reinsurance form (shown as separate captions in this report) and financial guaranty form (included in the structured finance financial guaranty insurance exposure totals in this note).

## **Residual Value Insurance**

The Company started providing insurance and reinsurance on aircraft RVI policies in the first quarter of 2017. RVI policies guarantee that a specific, properly maintained asset will have a specified value at a specified future date, or strike date. The Company seeks to limit its exposure to losses by underwriting aviation assets that it views as investment grade at inception, diversifying its insured portfolio across aircraft types and policy strike dates. This approach is designed to reduce the Company's exposure to the severe devaluation of a specific aircraft type or a temporary disruption in the overall aviation market. The RVI policy amount is set at or below a stressed forecasted value for the asset, so that the asset value would need to be below the stressed forecasted amount on the strike date for payment to be due under the RVI policy, with the loss under the RVI policy being the difference between the RVI amount and the amount recovered on the asset. Payment under the policy is contingent upon several factors, including, but not limited to, the asset being delivered to an agreed upon location in a satisfactory condition and without any liens, with deductions being made for any required repairs or improvements. The reinsurance market for this product is currently active, and the Company may choose to obtain additional reinsurance for its aircraft RVI reinsurance portfolio in the future in order to manage the size of the total portfolio and the exposure to specific aircraft types.

The Company's RVI transactions were executed in specialty insurance and reinsurance form.

## **Financial Guaranty**

The Company measures its financial guaranty exposure in terms of (a) gross and net par outstanding and (b) gross and net debt service.

The Company typically guarantees the payment of principal and interest when due. Since most of these payments are due in the future, the Company generally uses gross and net par outstanding as a proxy for its financial guaranty exposure. Gross par outstanding generally represents the principal amount of the insured obligation at a point in time. Net par outstanding equals gross par outstanding net of any third-party reinsurance. In the case of accreting (zero-coupon) obligations, the Company includes in its par outstanding calculation the impact of accretion to the reporting date.

Gross debt service outstanding represents the sum of all estimated future principal and interest payments on the obligations insured, on an undiscounted basis. Net debt service outstanding equals gross debt service outstanding net of any third-party reinsurance. In the case of accreting (zero-coupon) obligations, future debt service payments include the impact of accretion after the reporting date. The Company insures obligations supported by non-homogeneous pools of assets.

The Company calculates its debt service outstanding as the total estimated contractual future principal and interest due through maturity, regardless of whether the obligations may be called and regardless of whether, in the case of obligations where principal payments are due when an underlying asset makes a principal payment, the Company believes the obligations will be repaid prior to contractual maturity.

The calculation of debt service requires the use of estimates, which the Company updates periodically, including updated interest rates for variable rate insured obligations and other assumptions based on the characteristics of each insured obligation. Debt service is a measure of the estimated maximum potential exposure to insured obligations before considering the Company's various legal rights to the underlying collateral and other remedies available to it under its financial guaranty contract.

Actual debt service may differ from estimated debt service due to refundings, terminations, negotiated restructurings, prepayments, changes in interest rates on variable rate insured obligations and other factors.

The Company seeks to limit its exposure to losses by underwriting obligations that it views as investment grade at inception, diversifying its insured portfolio across asset classes and, in the structured finance portfolio, requiring rigorous subordination or collateralization requirements. Reinsurance may be used in order to reduce net exposure to certain insured transactions. While the Company has not provided new financial guaranty reinsurance in the recent past, it may do so again in the future. None of the Company's direct and assumed financial guaranty contracts are written in derivative form.

Public finance obligations covered by financial guaranty insurance assumed by the Company primarily consist 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 and toll roads.

Structured finance obligations covered by financial guaranty insurance assumed by the Company are generally issued by special purpose entities and backed by pools of assets having an ascertainable cash flow or market value or other specialized financial obligations. The Company also provides specialty insurance and reinsurance on transactions without special purpose entities but with similar risk profiles to its structured finance exposures written in financial guaranty form.

### **Significant Risk Management Activities**

The Portfolio Risk Management Committee of the Company's indirect parent, AGL, which includes members of AGL's senior management and senior risk and surveillance officers, establishes Assured Guaranty-wide credit policy for Assured Guaranty's direct and assumed business. It implements specific underwriting procedures and limits for Assured Guaranty and allocates underwriting capacity among AGL's subsidiaries, including the Company. The Portfolio Risk Management Committee is responsible for enterprise risk management for Assured Guaranty and focuses on measuring and managing credit, market and liquidity risk for Assured Guaranty. All transactions in new asset classes or new jurisdictions must be approved by this committee. The Company's risk management committee conducts an in-depth review of the Company's insured portfolio, focusing on varying portions of the portfolio at each meeting. It reviews and may revise internal ratings assigned to the insured transactions and review sector reports, monthly product line surveillance reports and compliance reports.

All transactions in the insured portfolio are assigned internal credit ratings by the relevant underwriting committee at inception, which credit ratings are updated by the relevant risk management committee based on changes in transaction credit quality. As part of the surveillance process, the Company monitors trends and changes in transaction credit quality and recommends such remedial actions as may be necessary or appropriate; however, most loss mitigation occurs at the Company's ceding companies, which are primarily liable for the Company's assumed obligations. The Company's ceding companies, including the Company's affiliates Assured Guaranty Municipal Corp. (AGM) and Assured Guaranty Corp. (AGC), also develop strategies to enforce their contractual rights and remedies and to mitigate their losses, engage in negotiation discussions with transaction participants and, when necessary, manage the litigation proceedings. The Company generally assumes its proportionate share of any net benefits realized by the ceding company for loss mitigation strategies.

### **Surveillance Categories**

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

The Company monitors its insured portfolio and refreshes its internal credit ratings on individual exposures in quarterly, semi-annual or annual cycles based on the Company's view of the exposure's credit quality, loss potential, volatility and sector. Ratings on exposures in sectors identified as under the most stress or with the most potential volatility are reviewed every quarter, although the Company may also review a rating in response to developments impacting the credit when a ratings review is not scheduled. For assumed exposures, the Company may use the ceding company's credit ratings of transactions where it is impractical for it to assign its own rating.

Exposures identified as BIG are subjected to further review to determine the probability of a loss. See Note 5, Losses, for additional information. Surveillance personnel then assign each BIG transaction to the appropriate BIG surveillance category based upon whether a future loss is expected and whether a claim has been paid. The Company uses a tax-equivalent yield to calculate the present value of projected payments and recoveries and determine whether a future loss is expected in order to assign the appropriate BIG surveillance category to a transaction. For financial statement measurement purposes, the Company uses risk-free rates, which are determined each quarter, to calculate the expected loss.

More extensive monitoring and intervention is employed for all BIG surveillance categories, with internal credit ratings reviewed quarterly. For purposes of determining the appropriate surveillance category, the Company expects "future

losses” on a transaction when the Company believes there is at least a 50% chance that, on a present value basis, it will in the future pay claims on that transaction that will not be fully reimbursed. The three BIG categories are:

- BIG Category 1: Below-investment-grade transactions showing sufficient deterioration to make future losses possible, but for which none are currently expected.
- BIG Category 2: Below-investment-grade transactions for which future losses are expected but for which no claims (other than liquidity claims, which are claims that the Company expects to be reimbursed within one year) have yet been paid.
- BIG Category 3: Below-investment-grade transactions for which future losses are expected and on which claims (other than liquidity claims) have been paid.

Unless otherwise noted, ratings disclosed herein on the Company's insured portfolio reflect its internal credit ratings.

**Net Exposure (1)  
by Internal Rating  
As of December 31, 2019**

Rating Category	Life Insurance Transactions		RVI		Financial Guaranty		Total	
	Net Exposure	%	Net Exposure	%	Net Exposure	%	Net Exposure	%
(dollars in thousands)								
AAA	\$ —	—%	\$ —	—%	\$ 46	—%	\$ 46	—%
AA	897,585	100.0	—	—	19,935	12.5	917,520	70.5
A	—	—	—	—	72,347	45.0	72,347	5.6
BBB	—	—	243,233	100.0	68,290	42.5	311,523	23.9
BIG (2)	—	—	—	—	8	—	8	—
Total net exposure	<u>\$ 897,585</u>	<u>100.0%</u>	<u>\$ 243,233</u>	<u>100.0%</u>	<u>\$ 160,626</u>	<u>100.0%</u>	<u>\$ 1,301,444</u>	<u>100.0%</u>

**Net Exposure (1)  
by Internal Rating  
As of December 31, 2018**

Rating Category	Life Insurance Transactions		RVI		Financial Guaranty		Total	
	Net Exposure	%	Net Exposure	%	Net Exposure	%	Net Exposure	%
(dollars in thousands)								
AAA	\$ —	—%	\$ —	—%	\$ 60,989	26.5%	\$ 60,989	5.0%
AA	762,641	100.0	—	—	10,545	4.6	773,186	63.9
A	—	—	—	—	83,463	36.4	83,463	6.9
BBB	—	—	218,059	100.0	74,561	32.5	292,620	24.2
BIG (2)	—	—	—	—	11	—	11	—
Total net exposure	<u>\$ 762,641</u>	<u>100.0%</u>	<u>\$ 218,059</u>	<u>100.0%</u>	<u>\$ 229,569</u>	<u>100.0%</u>	<u>\$ 1,210,269</u>	<u>100.0%</u>

- (1) Exposure for life insurance transactions and RVI is shown net of any reinsurance ceded. For financial guaranty contracts, exposure is the par outstanding of the insured obligation net of any reinsurance ceded.
- (2) BIG exposure relates to one risk at both December 31, 2019 and December 31, 2018, which relates to general obligation bonds. A risk represents the aggregate of the financial guaranty policies that share the same revenue source for purposes of making debt service payments.

## Gross Exposure

Sector	As of December 31, 2019	As of December 31, 2018
	(in thousands)	
Life insurance transactions	\$ 1,045,851	\$ 880,138
RVI	398,285	339,853
Financial guaranty U.S. public finance	142,945	146,117
Financial guaranty U.S. structured finance	487,681	459,452
Total gross exposure	<u>\$ 2,074,762</u>	<u>\$ 1,825,560</u>

## Net Exposure (1) by Sector

Sector	As of December 31, 2019	As of December 31, 2018
	(in thousands)	
Life insurance transactions (2)	\$ 897,585	\$ 762,641
RVI	243,233	218,059
Financial guaranty U.S. public finance:		
General obligation	75,159	77,597
Investor-owned utilities	45,000	45,000
Municipal utilities	8,360	8,560
Tax-backed	7,992	8,060
Transportation	6,434	6,900
Financial guaranty U.S. public finance	<u>142,945</u>	<u>146,117</u>
Financial guaranty U.S. structured finance:		
Commercial receivables	5,681	10,509
Other asset-backed tax credit	12,000	72,943
Financial guaranty U.S. structured finance	<u>17,681</u>	<u>83,452</u>
Total net exposure	<u>\$ 1,301,444</u>	<u>\$ 1,210,269</u>

- (1) Exposure for life insurance transactions and RVI is shown net of any reinsurance ceded. For financial guaranty contracts, exposure is the par outstanding of the insured obligation net of any reinsurance ceded.
- (2) The life insurance transactions net exposure is projected to increase to approximately \$1.0 billion by December 31, 2023.

Actual maturities of insured obligations could differ from contractual maturities because borrowers have the right to call or prepay certain obligations. The expected maturities of financial guaranty structured finance obligations are, in general, considerably shorter than the contractual maturities for such obligations.

**Expected Amortization of  
Net Exposure  
As of December 31, 2019**

	<b>Life Insurance Transactions (1)</b>	<b>RVI</b>	<b>Financial Guaranty U.S. Public Finance</b>	<b>Financial Guaranty U.S. Structured Finance</b>	<b>Total</b>
	(in thousands)				
0 to 5 years	\$ (141,527)	\$ 71,862	\$ 80,786	\$ 16,428	\$ 27,549
5 to 10 years	90,639	150,226	25,415	1,253	267,533
10 to 15 years	338,847	21,145	17,981	—	377,973
15 to 20 years	609,626	—	18,763	—	628,389
Total net exposure	<u>\$ 897,585</u>	<u>\$ 243,233</u>	<u>\$ 142,945</u>	<u>\$ 17,681</u>	<u>\$ 1,301,444</u>

(1) The life insurance transactions net exposure is expected to continue to increase over the next four years.

**Additional Information Regarding the Financial Guaranty Portfolio**

The Company seeks to maintain a diversified portfolio of insured financial guaranty obligations designed to spread its financial guaranty risk across a number of geographic areas, all in the U.S.

**Financial Guaranty Portfolio  
Geographic Distribution of  
Net Par Outstanding  
As of December 31, 2019**

	<b>Number of Risks</b>	<b>Net Par Outstanding (dollars in thousands)</b>	<b>Percent of Total Net Par Outstanding</b>
U.S. public finance:			
Illinois	6	\$ 62,625	39.0%
Michigan	5	45,288	28.2
California	13	17,062	10.6
Other states (1)	31	17,970	11.2
Total U.S. public finance	55	142,945	89.0
U.S. structured finance (multiple states)	3	17,681	11.0
Total	58	\$ 160,626	100.0%

(1) No individual state net exposure is greater than 3.4% of financial guaranty net par outstanding.

**Financial Guaranty  
Debt Service Outstanding**

	<b>Gross Debt Service Outstanding</b>		<b>Net Debt Service Outstanding</b>	
	<b>December 31, 2019</b>	<b>December 31, 2018</b>	<b>December 31, 2019</b>	<b>December 31, 2018</b>
	(in thousands)			
U.S. public finance	\$ 196,060	\$ 205,937	\$ 196,060	\$ 205,937
U.S. structured finance	490,762	465,430	20,762	89,430
Total financial guaranty	<u>\$ 686,822</u>	<u>\$ 671,367</u>	<u>\$ 216,822</u>	<u>\$ 295,367</u>



#### **4. Premiums**

##### **Accounting Policies**

###### ***Life Insurance Transactions and RVI (Specialty Insurance and Reinsurance)***

The amount of unearned premium reserve at contract inception for premiums received upfront on RVI transactions is equal to the amount of cash received, and for premiums received in installments on on RVI and life insurance transactions, the unearned premium reserve is equal to the amount of contractual premiums currently due. The Company records earned premium received upfront on RVI contracts over the remaining contract period in proportion to the amount of insurance protection provided, and for premiums received in installments on RVI and life insurance transactions, when premiums are due. For life insurance transactions and RVI, premiums receivable consist of the amount of contractual premiums due.

###### ***Financial Guaranty Insurance***

Accounting for financial guaranty contracts that meet the scope exception under derivative accounting guidance are subject to industry specific guidance for financial guaranty insurance. The accounting for contracts that fall under the financial guaranty insurance definition are consistent whether contracts are written on a direct basis, assumed from another financial guarantor under a reinsurance treaty, or ceded to another insurer under a reinsurance treaty.

Premiums receivable represent the present value of contractual or expected future premium collections discounted using risk free rates. Unearned premium reserve represents unearned premium revenue that has not yet been recognized in the statement of operations.

The amount of unearned premium reserve at contract inception is determined as follows:

- For premiums received upfront on financial guaranty insurance contracts, unearned premium reserve is equal to the amount of cash received. Upfront premiums typically relate to public finance transactions.
- For premiums received in installments on financial guaranty insurance contracts, unearned premium reserve is the present value (discounted at risk free rates) of contractual premiums due. Installment premiums typically relate to structured finance transactions, where the insurance premium rate is determined at the inception of the contract but the insured par is subject to prepayment throughout the life of the transaction.

When the Company adjusts prepayment assumptions or expected premium collections, an adjustment is recorded to the unearned premium reserve, with a corresponding adjustment to the premium receivable. Premiums receivable are discounted at the risk-free rate at inception and such discount rate is updated only when changes to prepayment assumptions are made that change the expected date of final maturity.

The Company recognizes unearned premium reserve for financial guaranty insurance contracts as earned premium over the contractual period of the contract in proportion to the amount of insurance protection provided. As premium revenue is recognized, a corresponding decrease to the unearned premium reserve is recorded. The amount of insurance protection provided is a function of the insured par amount outstanding. Accordingly, the proportionate share of premium revenue recognized in a given reporting period is a constant rate calculated based on the relationship between the insured par amounts outstanding in the reporting period compared with the sum of each of the insured par amounts outstanding for all periods. When an insured financial obligation is retired before its maturity, the financial guaranty insurance contract is extinguished. Any nonrefundable unearned premium reserve related to that contract is accelerated and recognized as premium revenue. When a premium receivable balance is deemed uncollectible, it is written off to bad debt expense.

###### ***Reinsurance***

For assumed reinsurance contracts, net earned premiums reported in the Company's consolidated statements of operations are calculated based upon data received from ceding companies; however, some external ceding companies report premium data between 30 and 90 days after the end of the reporting period. The Company estimates net earned premiums for the lag period. Differences between such estimates and actual amounts are recorded in the period in which the actual amounts are determined. When installment premiums are related to assumed reinsurance contracts, the Company assesses the credit quality and liquidity of the ceding companies and the impact of any potential regulatory constraints to determine the collectability of such amounts. The accounting model used for premium and loss recognition is based on the underlying contracts of the ceding company as described below.

## Premium Components

Direct and assumed unearned premium reserve is recorded as a liability, and ceded unearned premium reserve is recorded as an asset. Direct, assumed and ceded earned premiums are presented together as net earned premiums in the statement of operations. See Note 7, Reinsurance, for a breakout of direct, assumed and ceded premiums. The components of net earned premiums are shown in the table below:

### Net Earned Premiums

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Life insurance transactions	\$ 2,351	\$ 2,107
RVI	3,241	2,354
Financial guaranty insurance:		
Scheduled net earned premiums	460	421
Accelerations from refundings	—	1
Accretion of discount on net premiums receivable	1	3
Financial guaranty insurance	461	425
Net earned premiums	<u>\$ 6,053</u>	<u>\$ 4,886</u>

### Components of Unearned Premium Reserve

	As of December 31, 2019			As of December 31, 2018		
	Gross	Ceded	Net	Gross	Ceded	Net
	(in thousands)					
Life insurance transactions and RVI	\$ 22,694	\$ 9,867	\$ 12,827	\$ 19,748	\$ 8,122	\$ 11,626
Financial guaranty:						
Deferred premium revenue	13,837	13,508	329	15,829	15,269	560
Contra-paid (1)	(1)	—	(1)	(1)	—	(1)
Unearned premium reserve	13,836	13,508	328	15,828	15,269	559
Total	<u>\$ 36,530</u>	<u>\$ 23,375</u>	<u>\$ 13,155</u>	<u>\$ 35,576</u>	<u>\$ 23,391</u>	<u>\$ 12,185</u>

(1) Contra paid reflects claim payments that are recorded when there is no loss and loss adjustment expense (LAE) reserve on a contract.

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

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Beginning of year	\$ 11,976	\$ 13,500
Less: Life insurance transactions and RVI premium receivable (specialty insurance and reinsurance)	610	458
Financial guaranty insurance premiums receivable	11,366	13,042
Gross written premiums, net of commissions	(368)	—
Gross premiums received, net of commissions	(1,919)	(1,869)
Adjustments:		
Changes in the expected term	217	(101)
Accretion of discount, net of commissions on assumed business	(133)	268
Cancellation of assumed reinsurance	—	26
Financial guaranty insurance premium receivable	9,163	11,366
Life insurance transactions and RVI premium receivable (specialty insurance and reinsurance)	2,073	610
December 31,	\$ 11,236	\$ 11,976

The Company has no installment premiums receivable denominated in currencies other than the U.S. dollar.

The timing and cumulative amount of actual collections may differ from expected collections in the table below due to factors such as counterparty collectability issues, accelerations, commutations, changes in expected lives and new business.

**Expected Collections of  
Financial Guaranty Insurance Gross Premiums Receivable,  
Net of Commissions on Assumed Business  
(Undiscounted)**

	As of December 31, 2019 (in thousands)
2020 (January 1 – March 31)	\$ 47
2020 (April 1 – June 30)	247
2020 (July 1 – September 30)	253
2020 (October 1 – December 31)	247
2021	987
2022	987
2023	987
2024	987
2025-2029	4,589
2030-2032	961
Total	\$ 10,292

The timing and cumulative amount of actual net earned premiums may differ from expected net earned premiums in the table below due to factors such as accelerations, commutations, changes in expected lives and new business.

## Scheduled Financial Guaranty Insurance Net Earned Premiums

	As of December 31, 2019 (in thousands)
2020 (January 1 – March 31)	\$ 30
2020 (April 1 – June 30)	29
2020 (July 1 – September 30)	29
2020 (October 1 – December 31)	27
Subtotal 2020	115
2021	88
2022	61
2023	33
2024	19
2025-2029	13
Net unearned premium reserve	329
Future accretion	1
Total future net earned premiums	\$ 330

## Selected Information for Financial Guaranty Insurance Policies Paid in Installments

	As of December 31, 2019	As of December 31, 2018
	(dollars in thousands)	
Premiums receivable, net of commission payable	\$ 9,163	\$ 11,366
Gross unearned premium reserve	13,525	15,412
Weighted-average risk-free rate used to discount premiums	2.2%	2.4%
Weighted-average period of premiums receivable (in years)	5.3	3.7

### 5. Losses

#### Expected Loss to Be Paid

Net expected loss to be paid includes estimates for specialty insurance and reinsurance, if applicable, as well as financial guaranty insurance. 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 for all contracts.

For financial guaranty contracts, 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, using current risk-free rates. Expected cash outflows and inflows are probability weighted cash flows that reflect 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. The Company updates the discount rates each quarter and reflects the effect of such changes in economic loss development. Net expected loss to be paid is defined as expected loss to be paid, net of amounts ceded to reinsurers.

For specialty insurance and reinsurance, the expected loss to be paid is equal to the reserve reported on the consolidated balance sheet (see below).

Economic loss development represents the change in net expected loss to be paid attributable to the effects of changes in assumptions based on observed market trends, changes in discount rates (for financial guaranty contracts), accretion of discount (for financial guaranty contracts) and the economic effects of loss mitigation efforts.

### **Loss Estimation Process**

The Company's loss reserve committee estimates expected loss to be paid for all contracts by reviewing analyses that consider various scenarios with corresponding probabilities assigned to them. Depending upon the nature of the risk, the Company's view of the potential size of any loss and the information available to the Company, that analysis may be based upon individually developed cash flow models, internal credit rating assessments, sector-driven loss severity assumptions and/or judgmental assessments. In the case of its assumed business, the Company may conduct its own analysis as just described or, depending on the Company's view of the potential size of any loss and the information available to the Company, the Company may use loss estimates provided by ceding insurers. The Company monitors the performance of its transactions with expected losses and each quarter the Company's loss reserve committee reviews and refreshes its loss projection assumptions, scenarios and the probabilities it assigns to those scenarios based on actual developments during the quarter and its view of future performance.

The exposures reinsured or insured by the Company may cover an extended period of time, in some cases over 30 years, and in most circumstances the Company has no right to cancel such reinsurance or insurance. As a result, the Company's estimate of ultimate loss on a policy is subject to significant uncertainty over the life of the reinsurance contract. Credit performance can be adversely affected by economic, fiscal and financial market variability, as well as more specific factors such as mortality and the market for assets covered by RVI insurance, over the life of the contracts.

The determination of expected loss to be paid is an inherently subjective process involving numerous estimates, assumptions and judgments by management, using both internal and external data sources with regard to frequency, severity of loss, economic projections, governmental actions, negotiations and other factors that affect credit performance. These estimates, assumptions and judgments, and the factors on which they are based, may change materially over a reporting period, and as a result the Company's loss estimates may change materially over that same period.

Changes in the Company's loss estimates for structured finance transactions generally will be influenced by factors impacting the performance of the assets supporting those transactions. Changes in the Company's loss estimates for life insurance exposures will be influenced by factors impacting mortality rates and changes in the Company's loss estimates for RVI exposures will be influenced by factors impacting the value of the covered assets. As of December 31, 2019 and 2018, there were no expected losses for structured finance, life insurance or RVI transactions.

The Company does not use traditional actuarial approaches to determine its estimates of financial guaranty expected losses. Actual losses will ultimately depend on future events or transaction performance and may be influenced by many interrelated factors that are difficult to predict. As a result, the Company's current projections of losses may be subject to considerable volatility and may not reflect the Company's ultimate claims paid.

The following table presents a roll forward of net expected loss to be paid for all contracts. The net expected loss and loss reserves of financial guaranty contracts included in the table has been discounted by the Company using the appropriate risk-free rates for U.S. dollar denominated obligations, that ranged from 0.00% to 2.45% with a weighted average of 1.57% as of December 31, 2019 and 0.00% to 3.06% with a weighted average of 2.46% as of December 31, 2018.

**Net Expected Loss to be Paid  
Roll Forward**

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Net expected loss to be paid, beginning of period (1)	\$ —	\$ 226
Economic loss development (benefit) due to:		
Accretion of discount	—	4
Changes in discount rates	—	(2)
Changes in timing and assumptions	2	(226)
Total economic loss development (benefit) (2)	2	(224)
Net (paid) recovered losses	(2)	(2)
Net expected loss to be paid, end of period (1)	\$ —	\$ —

- (1) There was no expected LAE to be paid as of December 31, 2019 and December 31, 2018.
- (2) See below for the roll forward of specialty insurance and reinsurance reserves and losses and LAE and reinsurance recoverable.

The Company had exposure to \$8 thousand as of December 31, 2019, compared with exposure of \$11 thousand as of December 31, 2018, of BIG U.S. public finance. Expected loss to be paid was de minimis as of both December 31, 2019 and December 31, 2018. The economic loss development across all sectors during 2019 was \$2 thousand, which was due primarily to the payment of assumed LAE expenses related to certain exposures. The economic benefit across all sectors during 2018 was \$225 thousand, which was due primarily to improved transaction performance. There was no net expected loss to be paid as of December 31, 2019 and December 31, 2018 for life insurance transactions and RVI contracts.

***Accounting Policies***

Loss and LAE reserve reported on the balance sheet relates only to direct and assumed reinsurance contracts. The corresponding reserve ceded to reinsurers is reported as reinsurance recoverable on unpaid losses and reported in other assets.

Under financial guaranty insurance accounting, the sum of unearned premium reserve and loss and LAE reserve represents the Company's stand ready obligation. At contract inception, the entire stand-ready obligation is represented by unearned premium reserve. A loss and LAE reserve for a financial guaranty contract is recorded only to the extent, and for the amount, that expected loss to be paid exceeds the unearned premium reserve on a contract by contract basis. As a result, the Company has expected loss to be paid on financial guaranty contracts that has not yet been expensed. Such amounts will be recognized in future periods as unearned premium reserve amortizes into income.

For specialty insurance and reinsurance, loss reserves consist of the estimates of unpaid reported losses and estimates for incurred but not reported losses. The reserve for unpaid reported losses, established by management based on reports from ceding companies, represents the estimated ultimate cost of events or conditions that have been reported to or specifically identified by the Company. Such reserves may be supplemented, as necessary, by management's estimates of reserves for losses incurred for which reports or claims have not been received. These estimates are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Such adjustments, if any, are reflected in the statement of operations in the period in which they are determined.

***Expected Loss to be Expensed For Financial Guaranty Insurance***

Expected loss to be expensed represents past or expected future financial guaranty net claim payments that have not yet been expensed. Such amounts will be expensed in future periods as unearned premium reserve amortizes into income on financial guaranty insurance policies. Expected loss to be expensed is the Company's projection of incurred losses that will be recognized in future periods, excluding accretion of discount. The Company had a de minimis amount of net expected loss to be expensed at December 31, 2019.

## Loss Activity and Components

The following table provides a reconciliation of the beginning and ending balances of specialty insurance and reinsurance reserves for losses and LAE and reinsurance recoverable. Losses incurred and paid are presented on a net basis.

### Rollforward of Specialty Insurance and Reinsurance Reserves for Losses and LAE

	Year Ended December 31, 2019	Year Ended December 31, 2018
	(in thousands)	
Balance as of January 1	\$ 71	\$ 72
Less: Reinsurance recoverable	71	72
Net loss and LAE reserve balance as of January 1	—	—
Incurred losses and LAE related to:		
Current year	—	—
Prior years	—	1
Total incurred losses and LAE	—	1
Loss and LAE (paid) recovered related to:		
Current year	—	—
Prior years	—	(1)
Total loss and LAE (paid) recovered	—	(1)
Net balance as of December 31	—	—
Plus: reinsurance recoverable	65	71
Balance as of December 31	<u>\$ 65</u>	<u>\$ 71</u>

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

### Loss and LAE Reported on the Consolidated Statements of Operations

	Loss (Benefit)	
	Year Ended December 31,	
	2019	2018
	(in thousands)	
Specialty insurance and reinsurance:		
Life	\$ —	\$ 1
Specialty insurance and reinsurance	—	1
Financial guaranty insurance		
U.S. public finance	2	1
U.S. structured finance	—	(151)
Financial guaranty insurance	2	(150)
Loss and LAE	<u>\$ 2</u>	<u>\$ (149)</u>

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

**Financial Guaranty Insurance BIG Transaction Loss Summary**  
**As of December 31, 2019 and 2018**

	<b>BIG Categories (1)</b>	
	<b>As of December 31, 2019</b>	<b>As of December 31, 2018</b>
	<b>(dollars in thousands)</b>	
Number of risks (2)	1	1
Remaining weighted-average contract period (in years)	2.3	2.4
Outstanding exposure:		
Par	\$ 8	\$ 11
Interest	1	2
Total	\$ 9	\$ 13
Expected cash outflows (inflows)	\$ —	\$ —
Potential recoveries	—	—
Subtotal	—	—
Discount	—	—
Present value of expected cash flows	\$ —	\$ —
Unearned premium reserve	\$ —	\$ —
Reserves	\$ —	\$ —

(1) All financial guaranty BIG transactions are classified as category 1.

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

## **6. Policy Acquisition Costs**

### ***Accounting Policy***

Policy acquisition costs that are directly related and essential to successful insurance contract acquisition, as well as ceding commission income and expense on ceded and assumed reinsurance contracts, are deferred and reported net.

Capitalized policy acquisition costs include the cost of underwriting personnel attributable to successful underwriting efforts. Management uses its judgment in determining the type and amount of costs to be deferred. The Company conducts an annual study to determine deferral rates.

Ceding commission expense on assumed reinsurance contracts and ceding commission income on ceded reinsurance contracts that are associated with premiums received in installments are calculated at their contractually defined commission rates, discounted consistent with premiums receivable for all future periods, and included in DAC, with a corresponding offset to net premiums receivable or reinsurance balances payable.

DAC is amortized in proportion to net earned premiums. Amortization of deferred policy acquisition costs includes the accretion of discount on ceding commission receivable and payable. When an insured obligation is retired early, the remaining related DAC is recognized at that time. Costs incurred for soliciting potential customers, market research, training, administration, unsuccessful acquisition efforts, and product development as well as all overhead type costs are charged to expense as incurred.



Expected losses and LAE, investment income, and the remaining costs of servicing the insured or reinsured business, are considered in determining the recoverability of DAC.

### Rollforward of Deferred Acquisition Costs

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Beginning of year	\$ 5,747	\$ 6,171
Deferrals	524	649
Amortization	(1,014)	(1,073)
End of year	<u>\$ 5,257</u>	<u>\$ 5,747</u>

## 7. Reinsurance

The Company assumes exposure (Assumed Business) and may cede portions of exposure it has insured or assumed (Ceded Business) in exchange for premiums, net of any ceding commissions. The Company historically entered into, and with respect to its new business continues to enter into, ceded reinsurance contracts in order to reduce the Company's net potential loss on ceded business to levels within the Company's risk tolerance.

### Accounting Policy

For business assumed and ceded, the accounting model used is the same model as would be used if the Company wrote the underlying contract directly instead of assuming it (see Note 4, Premiums and Note 5, Losses).

### Financial Guaranty Business

The Company assumes financial guaranty business from affiliated companies and third party insurers and reinsurers, primarily other monoline financial guaranty companies. Under these relationships, the Company assumes a portion of the ceding company's insured risk in exchange for a portion of the ceding company's premium for the insured risk (typically, net of a ceding commission). The Company, if required, secures its reinsurance obligations to its affiliated and non-affiliated ceding companies, typically by depositing in trust assets with a market value equal to its assumed liabilities calculated on a statutory basis of accounting.

The Company's facultative and treaty assumed agreements are generally subject to termination at the option of the ceding company:

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

Upon termination due to one of the above events, the Company typically would be required to return to the ceding company unearned premiums (net of ceding commissions) and loss reserves, calculated on a statutory basis of accounting, attributable to the Assumed Business (plus, in certain cases, an additional required amount), after which the Company would be released from liability with respect to such business.

The Company retrocedes financial guaranty business to a non-affiliated company. In the event that the reinsurer is unable to meet its obligations, the Company would remain liable for such defaulted amounts.

## Specialty Insurance and Reinsurance: Life Insurance Transactions and RVI

The Company assumes specialty business from third party insurers (Assumed Specialty Business). It also retrocedes some of its specialty business to third party reinsurers. A downgrade of AGRO's financial strength rating by S&P below "A" would require AGRO to post, as of December 31, 2019, an estimated \$0.1 million of collateral in respect of certain of its Assumed Specialty Business. A further downgrade of AGRO's S&P rating below A- would give the company ceding such business the right to recapture the business for AGRO's collateral amount, and, if also accompanied by a downgrade of AGRO's financial strength rating by A.M. Best Company, Inc. below A-, would also require AGRO to post, as of December 31, 2019, an estimated \$14 million of collateral in respect of a different portion of AGRO's Assumed Specialty Business. AGRO's ceded/retroceded contracts generally have equivalent provisions requiring the assuming reinsurer to post collateral and/or allowing AGRO to recapture the ceded/retroceded business upon certain triggering events, such as reinsurer rating downgrades.

### Effect of Reinsurance

The following table presents the components of premiums and losses reported in the consolidated statements of operations and the contribution of the Company's Assumed and Ceded Businesses (both financial guaranty and specialty). See Note 12, Related Party Transactions, for balances with affiliates.

#### Effect of Reinsurance on Statement of Operations

	Year Ended December 31,	
	2019	2018
	(in thousands)	
<b>Premiums Written:</b>		
Direct	\$ —	\$ 9,008
Assumed	9,022	2,330
Ceded	(1,999)	(4,163)
Net	<u>\$ 7,023</u>	<u>\$ 7,175</u>
<b>Premiums Earned:</b>		
Direct	\$ 489	\$ 376
Assumed	7,388	7,408
Ceded	(1,824)	(2,898)
Net	<u>\$ 6,053</u>	<u>\$ 4,886</u>
<b>Loss and LAE:</b>		
Assumed	\$ (2)	\$ (160)
Ceded	4	11
Net	<u>\$ 2</u>	<u>\$ (149)</u>

#### Exposure to Non-Affiliated Reinsurers (1)

	As of December 31, 2019	As of December 31, 2018
	(in thousands)	
Ceded premium payable, net of commissions	\$ 14,074	\$ 15,473
Ceded expected loss to be recovered (paid)	65	71
Ceded unearned premium reserve	23,375	23,391
Financial guaranty ceded par outstanding (2)	470,000	376,000
Specialty ceded exposure (see Note 3)	303,318	239,291

(1) There was no collateral posted by non-affiliate reinsurers as of December 31, 2019 and December 31, 2018. See Note 12, Related Party Transactions for information on affiliated reinsurers.

(2) All ceded par is rated investment grade as of December 31, 2019 and December 31, 2018.

## 8. Fair Value Measurement

The Company carries all of its investment portfolio 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 2019, no changes were made to the Company's valuation models that had, or are expected to have, a material impact on the Company's consolidated balance sheets or statements of operations and comprehensive income.

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

The categorization within the fair value hierarchy is determined based on whether the inputs to valuation techniques used to measure fair value are observable or unobservable. Observable inputs reflect market data obtained from independent 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's or liability's categorization is based on the lowest level of significant input to its valuation.

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

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

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

There was a transfer of a fixed-maturity security from Level 2 into Level 3 during 2019. There were no other transfers into or from Level 3 during the periods presented

## Carried at Fair Value

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

The fair value of fixed-maturity securities 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 using their pricing models, which take into account: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data, industry and economic events and sector groupings. Additional valuation factors that can be taken into account are nominal spreads and liquidity adjustments. The pricing services evaluate each asset class based on relevant market and credit information, perceived market movements, and sector news.

Benchmark yields have in many cases taken priority over reported trades for securities that trade less frequently or those that are distressed trades, and therefore may not be indicative of the market. The extent of the use of each input is dependent on the asset class and the market conditions. The valuation of fixed-maturity investments is more subjective when markets are less liquid due to the lack of market based inputs.

Short-term investments that are traded in active markets are classified within Level 1 in the fair value hierarchy and their value is based on quoted market prices. Securities such as discount notes are classified within Level 2 because these securities are typically not actively traded due to their approaching maturity and, as such, their cost approximates fair value.

As of December 31, 2019, the Company used models to price 14 securities with a fair value of \$25 million. All Level 3 securities were priced with the assistance of an independent third-party. The pricing is based on a discounted cash flow approach using the third-party's proprietary pricing models. The models use inputs such as projected prepayment speeds; severity assumptions; recovery lag assumptions; estimated default rates (determined on the basis of an analysis of collateral attributes, historical collateral performance, borrower profiles and other features relevant to the evaluation of collateral credit quality); home price appreciation/depreciation 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 security 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 have materially changed the expected timing of cash flows within these securities which is a significant factor in determining the fair value of the securities.

## Financial Instruments Carried at Fair Value

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

**Fair Value Hierarchy of Financial Instruments Carried at Fair Value  
As of December 31, 2019**

	Fair Value	Fair Value Hierarchy		
		Level 1	Level 2	Level 3
		(in thousands)		
Assets:				
Investment portfolio, available-for-sale:				
Fixed-maturity securities:				
Obligations of state and political subdivisions	\$ 139,966	\$ —	\$ 139,966	\$ —
U.S. government and agencies	11,318	—	11,318	—
Corporate securities	123,448	—	123,448	—
Mortgage-backed securities:				
RMBS	58,370	—	53,658	4,712
Commercial mortgage-backed securities (CMBS)	27,015	—	27,015	—
Asset-backed securities	20,386	—	—	20,386
Total fixed-maturity securities	380,503	—	355,405	25,098
Short-term investments	5,809	5,809	—	—
Total assets carried at fair value	\$ 386,312	\$ 5,809	\$ 355,405	\$ 25,098

**Fair Value Hierarchy of Financial Instruments Carried at Fair Value  
As of December 31, 2018**

	Fair Value	Fair Value Hierarchy			
		Level 1	Level 2	Level 3	
		(in thousands)			
Assets:					
Investment portfolio, available-for-sale:					
Fixed-maturity securities:					
Obligations of state and political subdivisions	\$ 134,590	\$ —	\$ 134,590	\$ —	
U.S. government and agencies	11,292	—	11,292	—	
Corporate securities	103,182	—	103,182	—	
Mortgage-backed securities:					
RMBS	57,994	—	54,059	3,935	
CMBS	18,583	—	18,583	—	
Asset-backed securities	11,637	—	1,579	10,058	
Total fixed-maturity securities	337,278	—	323,285	13,993	
Short-term investments	7,209	2,213	4,996	—	
Total assets carried at fair value	\$ 344,487	\$ 2,213	\$ 328,281	\$ 13,993	

**Changes in Level 3 Fair Value Measurements**

The tables below present a roll forward of the Company's Level 3 financial instruments carried at fair value on a recurring basis during the years ended December 31, 2019 and 2018.

**Rollforward of Level 3 Fair Value Assets  
At Fair Value on a Recurring Basis  
Year Ended December 31, 2019**

	Fixed-Maturity Securities	
	RMBS	Asset-Backed Securities
	(in thousands)	
Fair value as of December 31, 2018	\$ 3,935	\$ 10,058
Total pretax realized and unrealized gains/(losses) recorded in:		
Net income (loss)	385 (1)	(1) (1)
Other comprehensive income (loss)	1,011	116
Purchases	—	10,340
Settlements	(619)	(1,725)
Transfers into Level 3	—	1,598
Fair value as of December 31, 2019	\$ 4,712	\$ 20,386
Change in unrealized gains/(losses) included in other comprehensive income (OCI) related to financial instruments held as of December 31, 2019	\$ 1,030	\$ 114

**Rollforward of Level 3 Fair Value Assets  
At Fair Value on a Recurring Basis  
Year Ended December 31, 2018**

	<b>Fixed-Maturity Securities</b>	
	<b>RMBS</b>	<b>Asset-Backed Securities</b>
	<b>(in thousands)</b>	
Fair value as of December 31, 2017	\$ 5,587	\$ 7,308
Total pretax realized and unrealized gains/(losses) recorded in:		
Net income (loss)	586 (1)	17 (1)
Other comprehensive income (loss)	(435)	(159)
Purchases	—	7,281
Settlements	(1,803)	(4,389)
Fair value as of December 31, 2018	<u>\$ 3,935</u>	<u>\$ 10,058</u>
Change in unrealized gains/(losses) included in OCI related to financial instruments held as of December 31, 2018	<u>\$ (188)</u>	<u>\$ (134)</u>

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

## Level 3 Fair Value Disclosures

### Quantitative Information About Level 3 Fair Value Inputs At December 31, 2019

Financial Instrument Description (1)	Fair Value at December 31, 2019 (in thousands)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
<b>Assets:</b>				
Fixed-maturity securities:				
RMBS	\$ 4,712	Conditional prepayment rate	3.5% - 6.7%	6.6%
		Conditional default rate	2.1% - 3.5%	2.1%
		Loss severity	85.0% - 95.0%	94.8%
		Yield	5.2% - 5.4%	5.2%
Asset-backed securities (CLO)	20,386	Yield	2.6% - 3.1%	2.9%

### Quantitative Information About Level 3 Fair Value Inputs At December 31, 2018

Financial Instrument Description (1)	Fair Value at December 31, 2018 (in thousands)	Significant Unobservable Inputs	Range	Weighted Average as a Percentage of Current Par Outstanding
<b>Assets:</b>				
Fixed-maturity securities:				
RMBS	\$ 3,935	Conditional prepayment rate	4.5% - 6.5%	6.4%
		Conditional default rate	2.5% - 3.6%	2.6%
		Loss severity	85.0%	
		Yield	6.7% - 7.0%	7.0%
Asset-backed securities (Collateralized loan obligation)	10,058	Yield	4.3% - 4.5%	4.4%

(1) Discounted cash flow is used as the primary valuation technique for all financial instruments listed in these tables.

## Not Carried at Fair Value

### Financial Guaranty Insurance Contracts

Fair value is based on management's estimate of what a similarly rated financial guaranty insurance company would demand to acquire the Company's in-force book of financial guaranty insurance business. It is based on a variety of factors that may include pricing assumptions management has observed for portfolio transfers, commutations and acquisitions that have occurred in the financial guaranty market, as well as prices observed in the credit derivative market with an adjustment for illiquidity so that the terms would be similar to a financial guaranty insurance contract, and also includes adjustments for stressed losses, ceding commissions and return on capital. The Company classified the fair value of financial guaranty insurance contracts as Level 3.

### ***Loan Receivable from Affiliate***

The fair value of the loan receivable from an affiliate is determined by calculating the effect of changes in yield adjusted for a credit factor at the end of each reporting period. The fair value measurement of the loans receivable was classified as Level 3.

The carrying amount and estimated fair value of the Company's financial instruments not carried at fair value are presented in the following table.

**Fair Value of Financial Instruments Not Carried at Fair Value**

	As of December 31, 2019		As of December 31, 2018	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
(in thousands)				
<b>Assets (liabilities):</b>				
Loan receivable from affiliate	\$ 40,000	\$ 41,276	\$ 50,000	\$ 45,693
Other assets (1)	3,442	3,442	3,437	3,437
Financial guaranty insurance contracts (2)	(4,531)	(4,530)	(4,605)	(4,605)

(1) The Company's other assets consist of accrued interest, for which the carrying value approximates fair value.

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

## **9. Investments and Cash**

### **Accounting Policy**

The Company's investment portfolio consists of fixed-maturity and short-term investments, classified as available-for-sale at the time of purchase, and therefore carried at fair value. Changes in fair value for other-than-temporarily-impaired securities are bifurcated between credit losses and non-credit changes in fair value. The credit loss on other-than-temporarily-impaired securities is recorded in the statement of operations and the non-credit component of the change in fair value of securities, is recorded in OCI. For securities in an unrealized loss position where the Company has the intent to sell or it is more-likely-than-not that it will be required to sell the security before recovery, the entire impairment loss (i.e., the difference between the security's fair value and its amortized cost) is recorded in the consolidated statements of operations. Credit losses reduce the amortized cost of impaired securities. The amortized cost basis is adjusted for accretion and amortization (using the effective interest method) with a corresponding entry recorded in net investment income.

Realized gains and losses on sales of investments are determined using the specific identification method. Realized loss includes amounts recorded for other-than-temporary impairments (OTTI) on debt securities and the declines in fair value of securities for which the Company has the intent to sell the security or inability to hold until recovery of amortized cost.

For mortgage-backed securities, and any other holdings for which there is prepayment risk, prepayment assumptions are evaluated and revised as necessary. Any necessary adjustments due to changes in effective yields and maturities are recognized in net investment income using the retrospective method.

Short-term investments, which are those investments with a maturity of less than one year at time of purchase, are carried at fair value and include amounts deposited in money market funds.

Cash consists of cash on hand and demand deposits. The Company has no restricted cash as of December 31, 2019 and 2018.



## Assessment for Other-Than Temporary Impairments

The Company has a formal review process to determine OTTI for securities in its investment portfolio where there is no intent to sell and it is not more-likely-than-not that it will be required to sell the security before recovery. Factors considered when assessing impairment include:

- a decline in the market value of a security by 20% or more below amortized cost for a continuous period of at least six months;
- a decline in the market value of a security for a continuous period of 12 months;
- recent credit downgrades of the applicable security or the issuer by rating agencies;
- the financial condition of the applicable issuer;
- whether loss of investment principal is anticipated; and
- whether scheduled interest payments are past due.

The Company assesses the ability to recover the amortized cost by comparing the net present value of projected future cash flows with the amortized cost of the security. If the security is in an unrealized loss position and its net present value is less than the amortized cost of the investment, an OTTI is recorded. The net present value is calculated by discounting the Company's estimate of projected future cash flows at the effective interest rate implicit in the debt security at the time of purchase. The Company's estimates of projected future cash flows are driven by assumptions regarding probability of default and estimates regarding timing and amount of recoveries associated with a default. The Company develops these estimates using information based on historical experience, credit analysis and market observable data, such as industry analyst reports and forecasts, sector credit ratings and other relevant data. For mortgage-backed and asset backed securities, cash flow estimates also include prepayment and other assumptions regarding the underlying collateral such as default rates, recoveries and changes in value. The assumptions used in these projections require the use of significant management judgment. If management's assessment changes in the future, the Company may ultimately record a loss after having originally concluded that the decline in value was temporary.

In addition to the factors noted above, the Company also seeks advice from its outside investment managers.

## Net Investment Income and Realized Gains (Losses)

Net investment income is a function of the yield that the Company earns on invested assets and the size of the portfolio. The investment yield is a function of market interest rates at the time of investment as well as the type, credit quality and maturity of the invested assets. Accrued investment income on the investment portfolio and the loan receivable from affiliate, which are recorded in other assets, was \$3.4 million as of both December 31, 2019 and December 31, 2018.

### Net Investment Income

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Income from fixed-maturity securities and short-term investments	\$ 12,242	\$ 11,388
Interest income from loan receivable from affiliate (see Note 12)	2,771	3,043
Gross investment income	15,013	14,431
Investment expenses	(322)	(232)
Net investment income	\$ 14,691	\$ 14,199

### Net Realized Investment Gains (Losses)

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Gross realized gains on available-for-sale securities	\$ 121	\$ 94
Gross realized losses on available-for-sale securities	(351)	(1,138)
OTTI	—	—
Net realized investment gains (losses)	<u>\$ (230)</u>	<u>\$ (1,044)</u>

There was de minimis amount of credit losses as of both December 31, 2019 and December 31, 2018 for fixed-maturity securities for which the Company has recognized an OTTI and where the portion of the fair value adjustment related to other factors was recognized in OCI.

### Investment Portfolio

As of December 31, 2019, the majority of the investment portfolio is managed by one outside manager. The Company has established detailed guidelines regarding credit quality, exposure to a particular sector and exposure to a particular obligor within a sector. The managed portfolio must maintain a minimum average rating of A+ by S&P or A1 by Moody's.

### Fixed-Maturity Securities and Short-Term Investments by Security Type As of December 31, 2019

Security Type	Percent of Total (1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI (2) Pre-Tax Gain (Loss) on Securities with OTTI	Weighted Average Credit Rating (3)
(dollars in thousands)							
Fixed-maturity securities:							
Obligations of state and political subdivisions	35%	\$ 129,136	\$ 10,848	\$ (18)	\$ 139,966	\$ —	AA
U.S. government and agencies	3	10,131	1,187	—	11,318	—	AA+
Corporate securities	32	117,812	5,645	(9)	123,448	—	A-
Mortgage-backed securities (4):							
RMBS	15	55,534	2,839	(3)	58,370	840	AA
CMBS	7	25,598	1,417	—	27,015	—	AAA
Asset-backed securities	6	20,394	18	(26)	20,386	—	AAA
Total fixed-maturity securities (5)	98	358,605	21,954	(56)	380,503	840	AA-
Short-term investments	2	5,809	—	—	5,809	—	AAA
Total investment portfolio	100%	<u>\$ 364,414</u>	<u>\$ 21,954</u>	<u>\$ (56)</u>	<u>\$ 386,312</u>	<u>\$ 840</u>	<u>AA-</u>

**Fixed-Maturity Securities and Short-Term Investments**  
**by Security Type**  
**As of December 31, 2018**

Security Type	Percent of Total (1)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	AOCI Pre-Tax Gain (Loss) on Securities with OTTI	Weighted Average Credit Rating (3)
(dollars in thousands)							
<b>Fixed-maturity securities:</b>							
Obligations of state and political subdivisions	39%	\$ 130,587	\$ 4,294	\$ (291)	\$ 134,590	\$ —	AA
U.S. government and agencies	3	10,258	1,044	(10)	11,292	—	AA+
Corporate securities	31	104,740	750	(2,308)	103,182	—	A
<b>Mortgage-backed securities (4):</b>							
RMBS	17	57,864	513	(383)	57,994	(31)	AA
CMBS	5	18,486	124	(27)	18,583	—	AAA
Asset-backed securities	3	11,781	—	(144)	11,637	—	AAA
<b>Total fixed-maturity securities (5)</b>	<b>98</b>	<b>333,716</b>	<b>6,725</b>	<b>(3,163)</b>	<b>337,278</b>	<b>(31)</b>	<b>AA-</b>
Short-term investments	2	7,209	—	—	7,209	—	AAA
<b>Total investment portfolio</b>	<b>100%</b>	<b>\$ 340,925</b>	<b>\$ 6,725</b>	<b>\$ (3,163)</b>	<b>\$ 344,487</b>	<b>\$ (31)</b>	<b>AA-</b>

(1) Based on amortized cost.

(2) Accumulated OCI (AOCI).

(3) Ratings 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 primarily consists of high-quality, liquid instruments.

(4) U.S. government-agency obligations were approximately 76% of mortgage backed securities as of December 31, 2019 and 75% as of December 31, 2018, based on fair value.

(5) 1.0% and 1.2% of fixed-maturity securities are rated BIG as of December 31, 2019 and December 31, 2018, respectively, 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.

The following tables present the fair value of the Company's available-for-sale portfolio of obligations of state and political subdivisions as of December 31, 2019 and December 31, 2018 by state.

**Fair Value of Available-for-Sale Portfolio of  
Obligations of State and Political Subdivisions  
As of December 31, 2019 (1)**

State	State General Obligation	Local General Obligation	Revenue Bonds	Total Fair Value	Amortized Cost	Average Credit Rating
(in thousands)						
California	\$ 2,354	\$ 1,576	\$ 22,633	\$ 26,563	\$ 24,588	AA-
Texas	2,323	3,329	19,189	24,841	22,931	AA
New York	—	3,408	15,363	18,771	16,928	AA+
Washington	—	—	9,361	9,361	8,786	AA-
Pennsylvania	4,345	—	2,956	7,301	6,923	AA-
Virginia	—	—	6,113	6,113	5,635	AA+
District of Columbia	578	—	4,405	4,983	4,676	AA
Florida	—	—	4,459	4,459	3,925	A+
Oregon	—	2,726	1,173	3,899	3,742	AAA
Oklahoma	—	—	2,377	2,377	2,249	A+
All others	2,283	1,205	16,632	20,120	18,512	AA-
Total	<u>\$ 11,883</u>	<u>\$ 12,244</u>	<u>\$ 104,661</u>	<u>\$ 128,788</u>	<u>\$ 118,895</u>	AA

**Fair Value of Available-for-Sale Portfolio of  
Obligations of State and Political Subdivisions  
As of December 31, 2018 (1)**

State	State General Obligation	Local General Obligation	Revenue Bonds	Total Fair Value	Amortized Cost	Average Credit Rating
(in thousands)						
California	\$ 2,861	\$ 1,504	\$ 21,771	\$ 26,136	\$ 25,475	AA-
Texas	2,177	3,133	18,373	23,683	23,015	AA
New York	—	3,230	13,707	16,937	16,081	AA+
Washington	—	—	9,434	9,434	9,198	AA-
Florida	—	2,886	4,296	7,182	6,919	AA-
Pennsylvania	4,164	—	2,874	7,038	7,033	AA-
District of Columbia	562	—	5,850	6,412	6,340	AA
Virginia	—	—	5,859	5,859	5,720	AA+
Minnesota	—	—	2,786	2,786	2,733	AA-
Oklahoma	—	—	2,300	2,300	2,290	A+
All others	2,253	1,169	17,131	20,553	19,969	AA-
Total	<u>\$ 12,017</u>	<u>\$ 11,922</u>	<u>\$ 104,381</u>	<u>\$ 128,320</u>	<u>\$ 124,773</u>	AA

(1) Excludes \$11.2 million and \$6.3 million as of December 31, 2019 and 2018, respectively, of pre-refunded bonds, at fair value. The credit ratings are based on the underlying ratings and do not include any benefit from bond insurance.

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

**Revenue Bonds  
Sources of Funds**

Type	As of December 31, 2019		As of December 31, 2018	
	Fair Value	Amortized Cost	Fair Value	Amortized Cost
(in thousands)				
Transportation	\$ 34,473	\$ 32,034	\$ 34,530	\$ 34,068
Water and sewer	23,741	21,335	22,703	21,592
Higher education	13,763	12,940	14,821	14,506
Tax backed	11,758	10,666	9,117	8,603
Municipal utilities	10,842	10,221	13,397	13,125
Healthcare	9,721	9,004	9,813	9,615
Other	363	365	—	—
Total	<u>\$ 104,661</u>	<u>\$ 96,565</u>	<u>\$ 104,381</u>	<u>\$ 101,509</u>

The following tables summarize, for all fixed-maturity 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 December 31, 2019**

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
(dollars in thousands)						
Obligations of state and political subdivisions	\$ 3,142	\$ (18)	\$ —	\$ —	\$ 3,142	\$ (18)
Corporate securities	1,220	(9)	—	—	1,220	(9)
Mortgage-backed securities						
RMBS	—	—	158	(3)	158	(3)
Asset-backed securities	2,500	—	7,854	(26)	10,354	(26)
Total	<u>\$ 6,862</u>	<u>\$ (27)</u>	<u>\$ 8,012</u>	<u>\$ (29)</u>	<u>\$ 14,874</u>	<u>\$ (56)</u>
Number of securities		<u>7</u>		<u>6</u>		<u>13</u>
Number of securities with OTTI		<u>—</u>		<u>—</u>		<u>—</u>

**Fixed-Maturity Securities**  
**Gross Unrealized Loss by Length of Time**  
**As of December 31, 2018**

	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
(dollars in thousands)						
Obligations of state and political subdivisions	\$ 2,096	\$ (8)	\$ 12,384	\$ (283)	\$ 14,480	\$ (291)
U.S. government and agencies	3,197	(10)	—	—	3,197	(10)
Corporate securities	9,371	(331)	31,836	(1,977)	41,207	(2,308)
Mortgage-backed securities						
RMBS	4,797	(55)	14,097	(328)	18,894	(383)
CMBS	4,290	(27)	—	—	4,290	(27)
Asset-backed securities	11,637	(144)	—	—	11,637	(144)
Total	<u>\$ 35,388</u>	<u>\$ (575)</u>	<u>\$ 58,317</u>	<u>\$ (2,588)</u>	<u>\$ 93,705</u>	<u>\$ (3,163)</u>
Number of securities (1)		<u>24</u>		<u>39</u>		<u>62</u>
Number of securities with OTTI		<u>1</u>		<u>—</u>		<u>1</u>

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

There were no securities in an unrealized loss position for 12 months or more as of December 31, 2019 with unrealized losses greater than 10% of book value. Of the securities in an unrealized loss position for 12 months or more as of December 31, 2018, two securities had unrealized losses greater than 10% of book value with unrealized loss of \$396 thousand. The Company has determined that the unrealized losses recorded as of December 31, 2019 and December 31, 2018 were not related to credit quality.

The amortized cost and estimated fair value of available-for-sale fixed-maturity securities by contractual maturity as of December 31, 2019 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 December 31, 2019**

	Amortized Cost	Estimated Fair Value
	(in thousands)	
Due within one year	\$ 27,356	\$ 27,584
Due after one year through five years	40,230	42,350
Due after five years through 10 years	117,735	125,630
Due after 10 years	92,152	99,554
Mortgage-backed securities:		
RMBS	55,534	58,370
CMBS	25,598	27,015
Total	<u>\$ 358,605</u>	<u>\$ 380,503</u>

Based on fair value, investments that are held in trust for the benefit of affiliated ceding insurers in accordance with statutory or contractual requirements totaled \$3.2 million and \$2.9 million as of December 31, 2019 and December 31, 2018, respectively.

No material investments of the Company were non-income producing for years ended December 31, 2019 and 2018, respectively.

## 10. Income Taxes

### Accounting Policy

The provision for income taxes consists of an amount for taxes currently payable and an amount for deferred taxes. Deferred income taxes are provided for temporary differences between the financial statement carrying amounts and tax bases of assets and liabilities, using enacted rates in effect for the year in which the differences are expected to reverse. A valuation allowance is recorded to reduce the deferred tax asset to an amount that is more likely than not to be realized.

The Company recognizes tax benefits only if a tax position is “more likely than not” to prevail.

### Overview

AGRO is not subject to any income, withholding or capital gains taxes under current Bermuda law. The Company has received an assurance from the Minister of Finance in Bermuda that, in the event of any taxes being imposed, AGRO will be exempt from taxation in Bermuda until March 31, 2035.

AGOUS and its subsidiaries AGRO and AG Intermediary Inc. file a consolidated U.S. federal income tax return (AGOUS consolidated return group). In addition, AGRO, a Bermuda domiciled company, has elected under Section 953(d) of the U.S. Internal Revenue Code to be taxed as a U.S. domestic corporation. Each company of the AGOUS consolidated return group will pay or receive its proportionate share of taxable expense or benefit as if it filed on a separate return basis with current period credit for net losses to the extent used in consolidation

### Tax Assets (Liabilities)

#### Deferred and Current Tax Assets (Liabilities)

	As of December 31, 2019	As of December 31, 2018
	(in thousands)	
Deferred tax assets (liabilities)	\$ (5,470)	\$ (1,599)
Current tax assets (liabilities) (1)	(112)	(77)

(1) Included in other assets or other liabilities on the consolidated balance sheets.

#### Components of Net Deferred Tax Assets (Liabilities)

	As of December 31,	
	2019	2018
	(in thousands)	
Deferred tax assets:		
Unearned premium reserves, net	\$ 831	\$ 948
Other	328	73
Total deferred income tax assets	1,159	1,021
Deferred tax liabilities:		
Unrealized appreciation on investments	4,599	748
Deferred acquisition costs	1,232	1,326
Market discount	714	469
Other	84	77
Total deferred income tax liabilities	6,629	2,620
Net deferred income tax asset (liability)	\$ (5,470)	\$ (1,599)

## Provision for Income Taxes

A reconciliation of the difference between the provision for income taxes and the expected tax provision at the U.S. marginal corporate income tax rate of 21% for 2019 and 2018 is presented below.

### Effective Tax Rate Reconciliation

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Expected tax provision (benefit)	\$ 3,065	\$ 2,553
Tax-exempt interest	(438)	(455)
Effect of provision to tax return filing adjustment	(175)	(240)
Other	(71)	19
Total provision (benefit) for income taxes	\$ 2,381	\$ 1,877
Effective tax rate	16.3%	15.4%

## Audits

AGOUS is not currently under audit and has open tax years of 2016 forward.

## 11. Insurance Company Regulatory Requirements

The following table summarizes the equity and income amounts reported to the Bermuda Monetary Authority (the Authority) for AGRO.

### Insurance Regulatory Amounts Reported

	Policyholders' Surplus		Net Income (Loss)	
	As of December 31,		Year Ended December 31,	
	2019	2018	2019	2018
	(in thousands)			
AGRO	\$ 410,012	\$ 383,308	\$ 12,217	\$ 10,280

## Basis of Regulatory Financial Reporting

The Company's ability to pay dividends depends, among other things, upon its financial condition, results of operations, cash requirements, compliance with rating agency requirements, and is also subject to restrictions contained in the insurance laws and related regulations of its country of domicile, Bermuda. Financial statements prepared in accordance with accounting practices prescribed or permitted by Bermuda insurance regulatory authorities differ from GAAP primarily due to the non-admission of certain assets in AGRO's statutory statements, that are admissible assets under GAAP.

## Dividend Restrictions and Capital Requirements

For AGRO, any distribution (including repurchase of shares) of any share capital, contributed surplus or other statutory capital that would reduce its total statutory capital by 15% or more of its total statutory capital as set out in its previous year's financial statements requires the prior approval of the Authority. Separately, dividends are paid out of an insurer's statutory surplus and cannot exceed that surplus. Furthermore, annual dividends cannot exceed 25% of total statutory capital and surplus as set out in its previous year's financial statements, which is \$103 million, without AGRO certifying to the Authority that it will continue to meet required margins. Based on the foregoing limitations, in 2020 AGRO has the capacity to (i) make capital distributions in an aggregate amount up to \$21 million without the prior approval of the Authority and (ii) declare and pay dividends in an aggregate amount up to approximately \$103 million as of December 31, 2019. Such dividend capacity is further limited by (i) the actual amount of AGRO's unencumbered assets, which amount changes from time to time



due in part to collateral posting requirements and which was approximately \$383 million as of December 31, 2019, and (ii) the amount of statutory surplus, which as of December 31, 2019 was \$273 million.

The Company did not declare or pay dividends during 2019 or 2018.

Under the Insurance Act, AGRO must ensure that the value of its general business statutory assets exceeds the amount of its general business statutory liabilities by an amount greater than the prescribed minimum solvency margin and each company's applicable enhanced capital requirement. The minimum solvency margin for Class 3A insurers is the greater of (i) \$1 million, or (ii) 20% of the first \$6 million of net premiums written; if in excess of \$6 million, the figure is \$1.2 million plus 15% of net premiums written in excess of \$6 million, or (iii) 15% of net discounted aggregate loss and loss expense provisions and other insurance reserves, or (iv) 25% of that insurer's applicable enhanced capital requirement reported at the end of its relevant year.

In addition, as a Class C long-term insurer, AGRO is required, with respect to its long-term business, to maintain a minimum solvency margin equal to the greater of (i) \$500,000, (ii) 1.5% of its assets or (iii) 25% its enhanced capital requirement reported at the end of the relevant year. For the purpose of this calculation, assets are defined as the total assets pertaining to its long-term business reported on the balance sheet in the relevant year less the amounts held in a segregated account. AGRO is also required to keep its accounts in respect of its long-term business separate from any accounts kept in respect of any other business and all receipts of its long-term business form part of its long-term business fund.

The Company is required to maintain available statutory capital and surplus at a level equal to or in excess of its applicable enhanced capital requirement, which is established by reference to either its Bermuda Solvency Capital Requirement model or an approved internal capital model.

## 12. Related Party Transactions

### Expense Sharing Agreements

The Company and various of its affiliates are parties to the Second Amended and Restated Service Agreement, effective as January 1, 2017 (as amended, the Group Service Agreement). The Company's affiliate, AG US Group Services Inc. (AG Services), a Delaware corporation, acts as the payroll company and employer for all U.S. personnel, and the central, dedicated service provider within the Assured Guaranty group. Under the Group Service Agreement, AG Services' employees make available to its Bermuda, U.S. and United Kingdom. affiliates, as applicable, equipment, insurance, reinsurance and such other services, including actuarial, marketing, underwriting, claims handling, surveillance, legal, corporate secretarial, information technology, human resources, accounting, tax, financial reporting and investment planning services. Expenses under the Group Service Agreement are allocated directly where appropriate and, where not appropriate, based upon an allocation of employee time and corresponding office overhead. The agreement provides for pre-funding by affiliates who are the largest consumers of group services, intercompany allocation of expenses and quarterly settlements and an express right of offset with regard to amounts owing between parties under the Group Service Agreement and other agreements between such parties.

The following table summarizes the allocated expenses from affiliated companies under the expense sharing agreements.

### Expenses Allocated From Affiliated Companies

	Year Ended December 31,	
	2019	2018
	(in thousands)	
Affiliated companies:		
AG Services	\$ 4,135	\$ 3,796
AGL	294	346
Total	\$ 4,429	\$ 4,142

The following table summarizes the amounts due to affiliated companies under the expense sharing agreements.

**Amounts Due To Affiliated Companies (1)**

	As of December 31,	
	2019	2018
	(in thousands)	
Affiliated companies		
AG Services	\$ 2,615	\$ 2,443
AGL	518	579
AGC	69	55
AG Re	39	20
AGM	16	1
Total	<u>\$ 3,257</u>	<u>\$ 3,098</u>

(1) Included in other liabilities on the consolidated balance sheets.

**Loan Receivable from Affiliate**

***Accounting Policy***

The loan receivable from affiliate was recorded at its principal amount. There was no discount or premium at the time of issuance of the loan.

***Loan to Assured Guaranty US Holdings Inc.***

On May 30, 2012, AGUS, a subsidiary of AGL, borrowed \$90 million from AGRO in order to fund a portion of the price of purchasing from Radian Asset Assurance Inc. a company that is now AGRO's affiliate Municipal Assurance Corp. Interest accrues on the unpaid principal amount of the loan at a rate of six-month LIBOR plus 3.00% per annum. During both 2019 and 2018, AGUS repaid \$10 million in outstanding principal on that loan as well as accrued and unpaid interest. In 2018 the parties agreed to extend the maturity date of the loan to November 2023. As of December 31, 2019, \$40 million remained outstanding. The Company recognized \$3 million of interest income during both years ended December 31, 2019 and 2018.

## Reinsurance Agreements

The Company assumes business from affiliated entities under certain reinsurance agreements. See below for material related party reinsurance balances.

The following table summarizes the affiliated components of each balance sheet item, where applicable:

	As of December 31,					
	2019			2018		
	AGC	AGM and AGE UK (3)	AG Re	AGC	AGM and AGE UK (3)	AG Re
	(in thousands)					
<b>Assets:</b>						
Premium receivable, net of commissions payable	\$ 16	\$ —	\$ 9,603	\$ 37	\$ —	\$ 11,195
DAC (1)	68	—	4,052	92	—	4,581
<b>Liabilities:</b>						
Unearned premium reserve	245	—	13,508	343	—	15,269
<b>Other information:</b>						
Assumed par outstanding	87,783	—	470,000	95,098	—	376,000

- (1) Represents assumed ceding commissions.  
(2) Included in other assets on the consolidated balance sheets.  
(3) Assured Guaranty (Europe) plc (AGE UK).

The following table summarizes the affiliated components of each statement of operations item, where applicable:

	Year Ended December 31,					
	2019			2018		
	AGC	AGM and AGE UK	AG Re	AGC	AGM and AGE UK	AG Re
	(in thousands)					
Revenues:						
Net earned premiums	\$ 99	\$ —	\$ 1,353	\$ 101	\$ 1	\$ 2,513
Expenses:						
Loss and LAE	2	—	—	(150)	—	—
Amortization of DAC	24	—	406	18	—	754

## Guaranty

AG Re provides an irrevocable guaranty to AGRO. Pursuant to the terms of the guaranty, upon demand by AGRO, to the extent AGRO is unable to satisfy any payment obligation, AG Re will make funds available to AGRO for the full payment of such payment obligation when it is due. AGRO has not made any demand to AG Re under this guaranty.

## 13. Commitments and Contingencies

### Leases

The Company's proportionate share of rent expense recognized in 2019 and 2018 was \$159 thousand and \$146 thousand, respectively.

## Legal Proceedings

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

## Accounting Policy

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

## 14. Other Comprehensive Income

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

**Changes in Accumulated Other Comprehensive Income by Component**  
**Year Ended December 31, 2019**

	Net Unrealized Gains (Losses) on Investments with no OTTI	Net Unrealized Gains (Losses) on Investments with OTTI	Total AOCI
		(in thousands)	
Balance, December 31, 2018	\$ 2,838	\$ (24)	\$ 2,814
Other comprehensive income (loss) before reclassifications	13,615	688	14,303
Less: Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(230)	—	(230)
Tax (provision) benefit	48	—	48
Total amount reclassified from AOCI, net of tax	(182)	—	(182)
Net current period other comprehensive income (loss)	13,797	688	14,485
Balance, December 31, 2019	\$ 16,635	\$ 664	\$ 17,299

**Changes in Accumulated Other Comprehensive Income by Component**  
**Year Ended December 31, 2018**

	Net Unrealized Gains (Losses) on Investments with no OTTI	Net Unrealized Gains (Losses) on Investments with OTTI (in thousands)	Total AOCI
Balance, December 31, 2017	\$ 9,435	\$ 3	\$ 9,438
Other comprehensive income (loss) before reclassifications	(7,422)	(27)	(7,449)
Less: Amounts reclassified from AOCI to:			
Net realized investment gains (losses)	(1,044)	—	(1,044)
Tax (provision) benefit	219	—	219
Total amount reclassified from AOCI, net of tax	(825)	—	(825)
Net current period other comprehensive income (loss)	(6,597)	(27)	(6,624)
Balance, December 31, 2018	\$ 2,838	\$ (24)	\$ 2,814

**15. Subsequent Events**

Subsequent events have been considered and disclosed if material through April 15, 2020, the date on which these financial statements were issued.

A novel coronavirus emerged in Wuhan, China in late 2019 and began to spread beyond China in early 2020. The virus is highly infectious and causes a coronavirus disease, COVID-19, that can be fatal. COVID-19 has been declared a pandemic by the World Health Organization, and its emergence and reactions to it, including various shelter-in-place and similar orders, are having a profound effect on the global economy and financial markets. The Company is evaluating the potential impact of COVID-19 and related developments, including developments in the global economy and financial markets and evolving governmental and private responses to the crisis, on its business and operations.

The Company began operating remotely on March 20, 2020, in accordance with its business continuity plan, and is providing the services and communications it normally would.